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In the Supreme Court of the United States

OCTOBER TERM, 1974

WILLIAM E. SIMON, SECRETARY OF THE TREASURY, ET AL., PETITIONERS

v.

EASTERN KENTUCKY WELFARE RIGHTS ORGANIZATION, ET AL.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

ROBERT H. BORK,
Solicitor General,
Department of Justice,
Washington, D.C. 20530.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

The Solicitor General, on behalf of the Secretary of the Treasury and the Commissioner of Internal Revenue, petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit in this case, but only if the Court grants the petition for a writ of certiorari which respondents, Eastern Kentucky Welfare Rights Organization, et al., are expected to file.

OPINIONS BELOW

The opinion of the district court (Appendix A, infra, pp. 1A–26A) is reported at 370 F. Supp. 325. The opinion of the court of appeals (Appendix B, *infra*, pp. 31A–57A is reported at 506 F.2d 1278.

JURISDICTION

The judgment of the court of appeals was entered on October 9, 1974 (Appendix C, *infra,* pp. 59A–60A). On December 6, 1974, the court of appeals denied Eastern Kentucky's petition for rehearing and also denied its suggestion for rehearing *en banc* (Appendix D, *infra,* pp. 61A–67A). On December 30, 1974, the Chief Justice extended the time for filing a petition for a writ of certiorari to and including March 8, 1975. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether the federal courts may review the correctness of revenue rulings and other similar administrative determinations made by the Department of the Treasury, in equitable suits brought by persons whose own tax liabilities are not at issue.

STATUTES INVOLVED

The relevant provisions of the Internal Revenue Code and the Declaratory Judgment Act are set forth in Appendix E, *infra,* pp. 68A–70A.

STATEMENT

This class action was brought by several individuals and a number of national and regional nonprofit health and welfare organizations on behalf of all indigent persons who are unable to pay for the costs of hospital care. The complaint alleged that the Secretary of the Treasury and the Commissioner of Internal Revenue erroneously recognized as tax-

exempt under Section 501(c)(3) of the Internal Revenue Code of 1954, private nonprofit hospitals that do not render free or below-cost medical service to indigents. Respondents sought broad declaratory and injunctive relief which would require the Treasury to withdraw the eligibility of such hospitals for rulings recognizing their tax-exempt status under Section 501(c)(3) of the Internal Revenue Code of 1954, and the deductibility of contributions to them under Section 170(c)(2) (J.A. 25–28).[1]

The circumstances which gave rise to this action concern the promulgation of two revenue rulings setting forth the Internal Revenue Service's position with regard to the exempt status of nonprofit hospitals.[2] The first of the two rulings, Revenue Ruling 56–185, 1956–1 Cum. Bull. 202, enumerated four general requirements which a hospital was required to satisfy to establish that it was exempt as a public charitable organization within the contemplation of Section 501(c)(3). One of the requirements included the condition that to the extent of its financial ability, the hospital serve those not able to pay for the services rendered.

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[1] "J.A." refers to the Joint Appendix filed in the court of appeals.

[2] Such rulings are published communications of the Commissioner of Internal Revenue to field offices, taxpayers, taxpayers' representatives, trade associations and others. The stated purpose of the Revenue Rulings system is to inform subordinate revenue officials of established policies and to make such information available to the public. Rev. Rul. 2, 1953–1 Cum. Bull. 484; Rev. Rul. 212, 1953–2 Cum. Bull. 449.

The Commissioner issued a second revenue ruling in 1969 modifying the earlier ruling. The later ruling, Revenue Ruling 69–545, 1969–2 Cum. Bull. 177, provided that a nonprofit hospital would also qualify for tax-exempt status if it operated a full-time emergency room which was open to all patients, regardless of their ability to pay, and if it accepted all patients who could pay the costs of their regular hospital care either directly or through some form of third-party reimbursement program, such as private health insurance, Medicare or Medicaid. Revenue Ruling 69–545 further stated that such a hospital would be recognized as tax-exempt even though non-emergency patients who could not meet the financial requirements for admission were ordinarily referred to another hospital in the community that did serve indigent patients.

In this action, respondents alleged that Revenue Ruling 69–545 was an erroneous interpretation of Section 501(c)(3) and that the Commissioner's issuance of the ruling had resulted in their inability to receive medical care from tax-exempt hospitals. They further alleged that the ruling was void since it had not been issued in accordance with the rule-making provisions of the Administrative Procedure Act requiring a public hearing and an opportunity for interested and affected persons to be heard. Accordingly, respondents sought a judicial declaration that the Treasury officials had acted unlawfully in recognizing the tax-exempt status of private nonprofit hospitals that did not admit and provide free or below cost medical care

to indigents, and an injunction requiring the Commissioner of Internal Revenue to revoke the exempt status of hospitals that did not furnish free care and to prohibit the future recognition of such hospitals as exempt organizations under Section 501(c)(3) (J.A. 25–28).

The Treasury officials moved to dismiss the complaint on the ground that the court lacked jurisdiction. The district court denied the motion to dismiss without an opinion (J.A. 32). Subsequently, upon the parties' cross motions for summary judgment, the district court granted summary judgment for respondents. It held that the court had jurisdiction to determine whether Revenue Ruling 69–545 was erroneous and that respondents had standing to maintain the action. The court further held that the revenue ruling at issue was not correct.

The court entered a declaratory judgment stating that the Treasury officials had misinterpreted Section 501(c)(3) in issuing Revenue Ruling 69–545 and that their attempted modification of the earlier ruling was void and without effect. The court also enjoined enforcement of the policy set forth in Revenue Ruling 69–545 and ordered that immediate steps ~~to~~ be taken to implement its order, including but not limited to revoking the voided portion of Revenue Ruling 69–545 and promulgating appropriate rulings to supersede the voided provisions. In view of its holding that the ruling was erroneous, the district court did not reach the issue whether the ruling was void because it was not issued in accordance with the notice and hearing

provisions of the Administrative Procedure Act (Appendix A, *infra*, pp. 1A–26A).

The court of appeals reversed. It held that Revenue Ruling 69–545 was not inconsistent with the legislative intent of Section 501(c)(3) and that the modification of the prior revenue ruling was proper. That court also concluded that the revenue ruling was interpretative, and thus not subject to the notice and hearing provisions of the Administrative Procedure Act, and that promulgation of the revenue ruling did not constitute an abuse of discretion (Appendix B, *infra*, pp. 31A–57A).

However, the court of appeals sustained the district court holding with respect to jurisdiction. It concluded that the defenses of standing, sovereign immunity, the Anti-Injunction Act, or the Declaratory Judgment Act were not applicable. It thereby concluded that the court did have jurisdiction to grant the relief requested (Appendix B, *infra*, pp. 36A–43A).

REASONS FOR GRANTING THE WRIT

We have been informed by counsel for respondents that they intend to file a petition for a writ of certiorari seeking review of the decision below holding that Revenue Ruling 69–545 is a correct interpretation of Section 501(c)(3) of the Code. We intend to oppose that petition. Should the Court grant respondents' petition, however, it should also grant the present petition, in order to preserve the Secretary of the Treasury's right to defend the court of appeals' judgment on the basis of the alternative contention

rejected by that court, that the federal courts may not review the correctness of revenue rulings in equitable actions brought by persons whose tax liability is not at issue.[3]

The jurisdictional holding of the court of appeals is contrary to Constitutional and statutory provisions generally reserving tax administrative authority to the Executive Branch under Congressional supervision,[4] as well as the Anti-Injunction Act (26 U.S.C. 7421(a)), the tax exception to the Declaratory Judgment Act (28 U.S.C. 2201–2202), and the doctrine of sovereign immunity, each of which precludes judicial review of such administrative actions by the Treasury. As the Court held in *Louisiana* v. *McAdoo*, 234 U.S. 627, 632, such general judicial review authority "would operate to disturb the whole revenue system of the Government and affect the revenues which arise therefrom." See also *United States* v. *American Friends Service Comm.*, No. 73–1791, October Term,

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[3] Although it would appear that a cross-petition is not necessary in order to raise an argument which does not seek to alter the judgment of the court of appeals, we are filing this conditional cross-petition out of an abundance of caution. See *Langnes* v. *Green*, 282 U.S. 531. Cf. *Strunk* v. *United States*, 412 U.S. 434; *National Labor Relations Board* v. *International Van Lines*, 409 U.S. 48, 52 and n. 4; *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375. Moreover, a cross-petition would not appear to be necessary where the objection to be raised is that the lower courts had no jurisdiction to consider the case. See *Peoria Ry. Co.* v. *United States*, 263 U.S. 528, 535–536; *Mattingly* v. *N.W. Virginia Railroad*, 158 U.S. 53, 57. See also *Matson Nav. Co.* v. *United States*, 284 U.S. 352, 359; *Capron* v. *Van Noorden*, 2 Cranch 126.

[4] See, *e.g.*, Article 1, Section 8, of the Constitution; 26 U.S.C. 7801, and 8001–8005.

1974, decided October 29, 1974. In addition, the jurisdictional holding of the court of appeals conflicts with the Tenth Circuit's recent refusals to exercise such general review authority over tax rulings in *Jr. C. of C., Rochester Inc., N.Y.* v. *U.S. Jaycees, Tulsa, Okla.*, 495 F2d 883, 888–889, certiorari denied, November 18, 1974, Nos 73–2025 and 73–2028; and *Cattle Feeders Tax Committee* v. *Shultz*, 504 F.2d 462.

The jurisdictional holding of the court of appeals invites anyone who disagrees with a published revenue ruling to sue in the District of Columbia, where the principal federal revenue officials are located, to enjoin them from taking any action consistent with such rulings. The serious threat to the orderly administration of the revenue laws presented by the decision below warrants review by this Court, if the petition of respondents is granted.

CONCLUSION

The petition for a writ of certiorari should be granted, but only if the Court grants the petition to be filed by respondents.

Respectfully submitted.

ROBERT H. BORK,
Solicitor General.

MARCH 1975.

APPENDIX A

United States District Court for the District of Columbia

Civil Action No. 1378–71

EASTERN KENTUCKY WELFARE RIGHTS ORGANIZATION, ET AL., PLAINTIFFS

v.

GEORGE P. SHULTZ, ET AL., DEFENDANTS

DECIDED DECEMBER 20, 1973

Marilyn G. Rose, Jeffrey B. Schwartz, Lauren H. Silver, Anthony Z. Roisman, Thomas Place, Peter Axelrod, Ralph Abascal, Jay-Allen Eisen and Ray Ratliff, Attorneys for Plaintiffs

John J. McCarthy, Donald J. Gavin, Milan D. Karlan and Harold H. Titus, Jr., United States Attorney, of Counsel, Attorneys for Defendants

Before BARRINGTON D. PARKER, District Judge

MEMORANDUM OPINION

In this class action against the Secretary of the Treasury and the Commissioner of Internal Revenue declaratory and injunctive relief is sought by the plaintiffs, comprising various health and welfare organizations and several private citizens, all alleging indigency and an inability to pay for hospital services. Called into question is the validity of an Internal Revenue Service (IRS or Service) policy, implemented by a revenue ruling, allowing private non-

profit hospitals to qualify as "charitable" institutions under the Internal Revenue Code of 1954 (Code) without requiring them to admit and provide free or reduced rate services to persons unable to pay. Jurisdiction of this action lies under 28 U.S.C. §§ 1331, 1340 and 1361; 28 U.S.C. §§ 2201 and 2202; and 5 U.S.C. §§ 702 and 703.

Plaintiffs seek a declaratory judgment that the defendants have acted unlawfully in granting tax exempt status to private nonprofit hospitals as "charitable" institutions under the Code and not requiring them to admit and provide free services to indigents. They also seek an injunction prohibiting the IRS from granting or continuing to extend tax benefits to such hospitals; to compel defendants to revoke their tax exempt status and to revoke the revenue ruling.[1]

The defendants initially moved to dismiss the complaint on the grounds that: the "Federal taxes" exemption to the Declaratory Judgment Act prevents the grant of such relief; the plaintiffs lack standing to sue; the issuance of revenue rulings may not be reviewed; the doctrine of sovereign immunity bars the suit, and; the ruling was interpretive in nature, therefore rendering the Administrative Procedure Act, 5 U.S.C. § 553 (APA), inapplicable. The motion was denied without opinion.

The matter is now presented on the plaintiffs' motion for summary judgment and the defendants' cross motion for summary judgment. The Court having considered the memoranda of points and authorities of the parties, the supporting affidavits, and the argument of counsel denies the defendants' motion and enters summary judgment on behalf of the plaintiffs.

[1] Plaintiffs also seek to compel the IRS to collect all taxes due and owing because of applications of this allegedly illegal program.

THE STATUTORY BACKGROUND

Section 501(a) and (c)(3)[2] of the Internal Revenue Code grants tax exempt status to charitable organizations; § 170(a) to (c)[3] permits individual and cor-

[2] The pertinent provisions of § 501 read as follows:

"(a) Exemption from taxation.—An organization described in subsection (c) or (d) or section 401(a) shall be exempt from taxation under this subtitle unless such exemption is denied under section 502, 503, or 504 . . .

"(c) List of exemption organizations.—The following organizations are referred to in subsection (a): . . .

"(3) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office."

[3] Section 170, dealing with deductions by taxpayers of Charitable contributions, in pertinent part states:

§ 170. Charitable, Etc., Contributions and Gifts

"(a) Allowance of deduction.

"(1) General rule.—There shall be allowed as a deduction any charitable contribution (as defined in subsection (c) payment of which is made within the taxable year. A charitable contribution shall be allowable as a deduction only if verified under regulations prescribed by the Secretary or his delegate * * *

"(c) Charitable contributions defined.—For purposes of this section, the term "charitable contribution" means a contribution or gift to or for the use of * * *

"(2) A corporation, trust, or community chest, fund, or foundation * * *

"(B) organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes or for prevention of cruelty to children or animals * * *

porate donors to deduct from their income tax returns contributions to certain entities organized and operated for charitable purposes. Hospitals as such have never been specifically listed in either §§ 501 or 170 as institutions to be accorded favorable tax consideration and they were able to do so only by qualifying as "charities" under the Code. Under § 7805(a) of the Code the Commissioner of Internal Revenue is empowered to promulgate necessary rules and regulations to implement the statute. These rulings set forth the official policy of the Service and are designed to guide taxpayers, the interested public and IRS officials in tax matters.[4]

Earlier IRS policy, as expressed in Revenue Ruling 56–185, which complemented § 501, provided in substance that hospitals could qualify as charities upon showing that, in addition to satisfying the other requirements of § 501, and even though permitted to assess full charges to patients capable of paying, they did not refuse treatment to indigent patients.[5] The

[4] *See* Footnote 9, *infra*.

[5] The portions of Revenue Ruling 56–185 most relevant to this suit are:

"In order for a hospital to establish that it is exempt as a public charitable organization within the contemplation of section 501(c)(3), it must, among other things, show that it meets the following general requirements . . .

"It must be operated to the extent of its financial ability for those not able to pay for the services rendered and not exclusively for those who are able and expected to pay. It is normal for hospitals to charge those able to pay for services rendered in order to meet the operating expenses of the institution, without denying medical care or treatment to others unable to pay. The fact that its charity record is relatively low is not conclusive that a hospital is not operated for charitable purposes to the full extent of its financial ability. It may furnish services at reduced rates which are below cost, and thereby render charity in that manner. It may also set aside earnings

current position of IRS which gives rise to this litigation is represented by Revenue Ruling 69–545 (Ruling). The striking feature of the 1969 ruling is the removal of that condition:

> "Revenue Ruling 56–185 is hereby modified to remove therefrom the requirements relating to caring for patients without charge or at rates below cost * * *"[6]

which it uses for improvements and additions to hospital facilities. It must not, however, refuse to accept patients in need of hospital care who cannot pay for such services. Furthermore, if it operates with the expectation of full payment from all those to whom it renders services, it does not dispense charity merely because some of its patients fail to pay for the services rendered."

[6] The pertinent provisions of Revenue Ruling 69–545 are:

"Section 501(c)(3) of the Code provides for exemption from Federal income tax of organizations organized and operated exclusively for charitable, scientific, or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual * * *

"To qualify for exemption from Federal income tax under section 501(c)(3) of the Code, a nonprofit hospital must be organized and operated exclusively in furtherance of some purpose considered "charitable" in the generally accepted legal sense of that term, and the hospital may not be operated, directly or indirectly, for the benefit of private interests.

"In the general law of charity, the promotion of health is considered to be a charitable purpose. Restatement (Second), Trusts, sec. 368 and sec. 372; IV Scott on Trusts (3rd ed. 1967), sec. 368 and sec. 372. A nonprofit organization whose purpose and activity are providing hospital care is promoting health and may, therefore, qualify as organized and operated in furtherance of a charitable purpose. If it meets the other requirements of section 501(c)(3) of the Code, it will qualify for exemption from Federal income tax under section 501(a) * * *

"Revenue Ruling 56–185, C.B. 1956–1, 202, sets forth requirements for exemption of hospitals under section 501(c)(3) more restrictive than those contained in this Revenue Ruling

Allegedly suffering detrimental effects from the Ruling, plaintiffs have leveled what can be fairly categorized as a two-pronged attack upon its validity. They assert that the promulgation of the Ruling was an *ultra vires* act in that it constituted an improper administrative alteration of Internal Revenue Code provisions, in contradiction of long standing tax policy and judicial interpretation. Alternatively, assuming *arguendo* that the defendants could have validly effectuated such a substantive change, they assert that the failure to grant them and other interested parties the opportunities to express their views, as required by the APA and the Fifth Amendment to the Constitution, demands that the ruling be vacated and its policy abandoned.

The defendants on the other hand contend first, that the plaintiffs lack standing to sue and fail to demonstrate a sufficient nexus between the action complained of and any alleged resulting injuries, and second, that the contested promulgation is outside the scope of judicial review. As to the merits, the Service maintains that the Ruling is rationally based and must be upheld.

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with respect to caring for patients without charge or at rates below cost. In addition, the fourth requirement of Revenue Ruling 56–185 is ambiguous in that it can be read as implying that the possibility of "shareholders" or "members" sharing in the assets of a hospital upon its dissolution will not preclude exemption of the hospital as a charity described in section 501(c)(3) of the Code. Section 1.501(c)(3)1(b)(4) of the regulations promulgated subsequent to Revenue Ruling 56–185 makes it clear, however, that an absolute dedication of assets to charity is a precondition to exemption under section 501 (c)(3) of the Code.

"Revenue Ruling 56–185 is hereby modified to remove therefrom the requirements relating to caring for patients without charge or at rates below cost. Furthermore, requirement four has been modified by section 1.501(c)(3)–1(b)(4) of the regulations."

STANDING

Under § 10 of the APA, 5 U.S.C. § 702, "[a] person suffering legal wrong because of agency action, or adversely affected or aggrieved by agency action within the meaning of a relevant statute, is entitled to judicial review thereof." This provision has been most recently interpreted in *United States* v. *Student Challenging Regulatory Agency Procedures (SCRAP)*, —— U.S. ——, 37 L. Ed. 2d 254 (1973). In that proceeding plaintiff organization, comprised of four law students, challenged the propriety of an Interstate Commerce Commission decision regarding an increase in railroad freight rates without having first prepared and considered an environmental impact statement in accordance with the National Environmental Policy Act. The Supreme Court found that the requirements of § 10 of the APA were satisfied by the litigants' allegations that the agency action would have adverse economic, recreational, environmental and aesthetic effects upon its individual members.

In its ruling the Court reaffirmed and expounded upon *Sierra Club* v. *Morton*, 405 U.S. 727 (1972), which established that a person could meet the APA standing requirements only when "the challenged action had caused him 'injury in fact,' and where the alleged injury was to an interest 'arguably within the zone of interests to be protected or regulated' by the statutes that the agencies were claimed to have violated." 405 U.S. at 733. By way of clarification, the *SCRAP* Court ruled that "[a] plaintiff must allege that he has been or will in fact be perceptively harmed by challenged agency action, not that he can imagine circumstances in which he could be affected by the

agency's action." —— U.S. ——, 37 L. Ed. 2d at 279.[7]

Plaintiffs, therefore, are confronted with a dual threshold test requiring of them a satisfactory demonstration that on basis of the pleadings first, they were injured as a result of the agency action, referred to as "injury in fact," and second, any such injury was to an interest protected by the law allegedly violated by the administrative action.

INJURY IN FACT

This Court has little difficulty in finding that under the *SCRAP* guidelines the plaintiffs have adequately demonstrated sufficient injury flowing from the issuance of Revenue Ruling 69–545 to afford them their day in Court.

Prior to that Ruling the policy of the Service in a very real sense, conferred a cognizable interest to indigents by requiring hospitals seeking tax advantages under the Code to give them special consideration. It simply defies common sense to contend that the plaintiffs have remained, or will remain, unaffected by a decision which all but strips from them basic and substantial benefits which had been previously nurtured by the government. Plaintiffs and other indi-

[7] As the Court noted, SCRAP's alleged injury was not, at first blush, easily demonstrable. It was alleged that the proposed rate increase would step up the use of nonrecyclable products thus requiring more natural resources to be expended from the Washington, D.C. area, where the litigants resided. This was enough, however, to overcome the courts skepticism of entertaining suits in which the pleadings were no more "than an ingenious academic exercise in the conceivable." —— U.S. ——, 27 L. Ed. 2d at 270.

It was significantly noted that APA standing is not restricted to those who have been "significantly" affected by agency action. —— U.S. ——, 37 L. Ed. 270–71, n. 14.

viduals have supplied affidavits[8] recounting incidents subsequent to the present Ruling where they were denied needed hospital attention because of indigency by institutions benefiting from the applicable Code provisions and Ruling.

The government points out, and the Court is not unmindful of the fact, that plaintiffs are hard pressed to demonstrate indisputably that their inability to secure medical services was a direct consequence of the Ruling. The circumstances surrounding this litigation, however, suggest that the defendants view of standing may be far too restrictive and unrealistic. It is obvious that while the poignant representations in the plaintiffs' affidavits do indeed reveal the severe health care crisis confronting the nation's poor, iron-clad documentation of a nexus between their tragic situation and hospital behavior towards indigents, as affected by the new Ruling, has not been and, in all probability, cannot be provided to the satisfaction of the criteria urged by the government. That observation notwithstanding, in light of the crucial significance with which hospitals regard their status as charities,[9] the

[8] *See* e.g., the following affidavits, filed on April 10, 1973: Eula Hall, Chairman, Health Committee, Eastern Kentucky Welfare Rights Organization; Lards Collins; Carolyn Block; Howard Linville, Treasurer, Association of Disabled Miners and Widows, Inc.; Rosezella Cook; Monica Hunter.

[9] Consider the statement of John Alexander McMahon, President of the American Hospital Association on Tax Reform Before the House Committee on Ways and Means, April 13, 1973, submitted as exhibit to Plaintiffs Motion for Summary Judgment. Mr. McMahon stated:

"Voluntary non profit hospitals are, in varying degrees, dependent upon charitable contributions * * *."

See also, "American United," Inc. v. Walters, 477 F. 2d 1169 (D.C. Cir. 1969), in which the court recognized the importance of tax benefits to "charitable" organizations:

"Because of the 'tax breaks' attendant to contributions to cor-

Court does not consider itself engaged in wild speculation by assuming or recognizing that the relaxation of the requirements for charitable classification would necessarily effect hospital policy, in this case care for indigents, upon which such a status had been earlier dependent.[10]

The Court finds the correlation between agency action and injury to plaintiffs to be at least as demonstrable as that which was accepted by the *SCRAP* Court and accordingly concludes that the initial "injury in fact" requirement under the APA has been met.

INJURY TO A PROTECTED INTEREST

Satisfaction of the standing test further requires that these plaintiffs show that any "injury in fact" has also affected an interest protected under the Internal Revenue Code.

porations qualifying under § 170(c) of the Code, qualification thereunder is a precious possession and removal from the Cumulative List, Organizations Described in Section 170(c) of the Internal Revenue Code of 1954 is a damaging—sometimes fatal—injury to the financial status of any 'charitable' organization." 477 F. 2d at 1177.

[10] This analysis is supported by the very purposes for the promulgation of Revenue Rulings. In an analysis of IRS procedure, a former Chief Counsel of the Service explained that the Rulings program, consisting of letters rulings (narrowly drawn to a particular set of facts) and the more general Revenue Rulings, is designed "to provide for certainty as to the tax consequences of contemplated transactions * * *." Rogovin, The Four R's: Regulations, Rulings, Reliance and Retroactivity A View From Within, 43 Taxes, 757, 763 (1965). These Rulings, according to Rogovin, have had a "broad impact on our national economy and on proper and reasonable tax administration." Rogovin, *supra* at 764.

It is clear that the IRS fully expects that policy promulgated by way of Revenue Rulings will effect the taxpaying public. It may be assumed, therefore, that activities relating to one's tax position will necessarily be influenced by such IRS rulings.

The government argues that the hospitals are the sole intended beneficiaries of the "charitable" Code provisions, claiming that the plaintiffs are "once removed" from the effects of the Code thereby leaving them outside the sphere of any interests obstensibly served by the relevant sections. This argument is too simplistic.

A review of the judicial and legislative background surrounding tax treatment for charities, as made applicable to hospitals in particular, demonstrates the weakness of their position and that plaintiffs do indeed fall within the zone of interests protected by the Code.

The prior Revenue Ruling, 56–185, represented a codification of previous Code interpretations which had been accepted and approved by the courts. In an earlier 1942 case, *Commissioner of Internal Revenue* v. *Battle Creek,* 216 F. 2d 405 (5th Cir. 1942), it was held that a sanitarium could properly be classified as a charitable institution under an earlier edition of the Revenue Code. As the court there explained at 406:

> "[i]t is also usual for hospitals and sanitariums to charge those able to pay for service rendered, in order to pay the expenses of the institution, while not denying treatment to others unable to pay anything. Such institutions are classed as charitable."

Intercity Hospital Association v. *Squire,* 56 F. Supp. 472 (W.D. Wash. 1944) involved the question of whether or not two hospitals were eligible for charitable treatment. The court ruled for the hospitals involved, placing significant emphasis upon the fact that "an extremely liberal rule prevailed concerning admittance of patients without funds."

This policy continued to receive favorable judicial recognition after it had been officially promulgated

by the IRS in Revenue Ruling 56–185. A decision of the Tax Court in *Sonora Community Hospital*, 46 T.C. 519 (1966), denied tax exempt status: "the mere fact that petitioner maintained a hospital does not in and of itself justify the conclusion that it was operated exclusively for charitable purposes." 46 T.C. at 525. In *Lorraine Avenue Clinic*, 31 T.C. 141 (1958), an insubstantial showing of aid to the poor proved fatal to the clinic's claim of being a charitable organization."[11]

Congressional developments are also significant. In 19–24 the Senate considered amending the "charitable" provisions of the then existing tax laws to enable health service organizations to automatically qualify for the relevant tax considerations. This proposal was not warmly received and was eventually abandoned.[12]

[11] *See also* 47 ALR 3d 1191 (1971) for an analysis of tax exempt organizations. The following observation was made with regard to hospitals:

"It is a usual practice for a hospital to charge patients who are able to pay for the services rendered in order to maintain the institution, pay off the indebtedness on its buildings, expand its facilities, or improve its services, while not denying treatment and care to patients who are unable to pay anything." 37 ALR 3d at 1223.

The annotation then surveyed numerous court rulings, both state and federal, which clearly revealed that charitable status, in the great majority of cases, depended upon the hospital showing, to varying quantitative degrees, that indigent patients had been admitted and treated. 37 ALR 3d pp. 1223–1234.

[12] A proposed change to a House Bill (H.R. 6715), under consideration by the Senate was introduced to allow for the automatic qualification of health organizations as charities. The amendment appears in parentheses:

"Any corporation, or community chest, fund, or foundation, organized and operated exclusively for religious, charitable (including preventive and constructive service for relief, rehabilitation, health, character building, and citizenship), scientific, literary, or educational purposes, etc." 65 Cong. Rec. 8171 (1924)

This attempt was prompted by a ruling of the Commissioner

The matter was most recently weighed in connection within the 1969 tax reform measures which included an attempt to confer hospitals with tax exempt status without regard to indigent service. The House version of the Tax Reform Act of 1969, H.R. 13270, which carried such a revision, was purportedly proposed to alleviate the "significant uncertainty as to the extent to which a hospital must accept patients who are unable to pay, in order to retain its exempt status." H. Rep. No. 413, 91st Cong., 1st Sess. 43 (1969).[13] This explanation, made public on August 4, 1969 by the Committee on Ways and Means, preceded by approximately two months the October 8, 1969 promulgation of Revenue Ruling 69–545. Shortly thereafter, on November 21, 1969, the Senate Committee on Finance acknowledged the new Ruling but explained why the Senate Bill would *not* incorporate this revision:

of Internal Revenue, II–2–1128, I.T. 1800, Int. Rev. Bull. 1–2 (1923), which required relief to the poor as a condition for charitable status. The amendment was withdrawn by its sponsor, Senator Willis. 65 Cong. Rec. 8173.

[13] H.R. 13270, 91st Cong. 1st Sess. authorized that "Section 501(c)(3) (relating to the definition of exempt organizations) is amended by inserting after 'animals', the phrase ', or for the providing of hospital care,'."

Hospitals had actively endorsed and advocated the passage of that revision. Julius M. Greisman, Attorney for the American Hospital Association, testifying before the House Committee on Ways and Means, felt that Revenue Ruling 56–185 was difficult to administer and urged that:

"* * * the tax law should be amended to provide that any hospital is exempt so long as it is operated principally for the purpose of providing hospital care."

Hearings on Tax Reform Act of 1969, H.R. 13270. Before House Committee on Ways and Means, 91st Cong. 1st Sess. 1425.

> "The Internal Revenue Service has, however, issued a ruling on October 8, 1969, indicating that hospitals, if they meet all the other requirements of § 501(c)(3), are exempt under that provision, whether or not they provide charitable services on a non-cost or low-cost basis. * * * The Committee deleted from the bill those provisions which would have conformed the Code to the result reached by the 1969 Ruling. The Committee decided to reexamine this matter in connection with pending legislation on Medicare and Medicaid." S. Rep. No. 91–552, 91st Cong. 1st Sess. 61 (1969).[14]

The Senate version, as indicated by the above cited report omitted the proposed House change. The House Conference Committee subsequently acquiesced in this determination:

> "The House Bill provides that hospitals, if they meet all the other requirements of Section 501 (c)(3), are exempt under that provision,

[14] The Senate Committee on Finance, in a Report of the Staff on Medicare and Medicaid, Problems, Issues and Alternatives considered in early 1970 the substance of Revenue Ruling 69–545. The staff noted that prior to the Ruling, IRS policy had provided a measure of protection against any unreasonable refusal by a nonprofit hospital to provide charitable and below-cost care:

"The staff strongly recommends revocation of Revenue Ruling 60–545 in light of the recent legislative history and continuation of the prior position of the Service until such time as Congress can devise an alternative approach establishing reasonable yardsticks of charitable service related to the financial capacity of a hospital. Such action by the Service would assist in protecting the availability of necessary hospital care to Medicare, Medicaid, and other poor patients." Medicare and Medicaid—Problems, Issues, and Alternatives. Report of the Staff to the Committee on Finance, U.S. Senate 91st Cong., 1st Sess. (Feb. 9, 1973).

> whether or not they provide charitable services on a non-cost or low-cost basis. The Senate amendment strikes out these provisions. The conference substitute . . . follows the Senate amendments." H. Rep. No. 91–782. 91st Cong., 1st Sess. 289–90 (1969).

The Tax Reform Act of 1969 contained no revisions on the subject.

This analysis, cursory as it may be, sufficiently highlights the point that Congress and the judiciary have consistently insisted that the application of §§ 501 and 170 to hospitals be conditioned upon a demonstration that ameliorative consideration be given poor people in need of hospitalization. The Court cannot accept the government's conclusion that these Code provisions are in no way intended to aid plaintiffs and those similarly situated. To do so one would have to disregard what has been held to be the underlying rationale for allowing charitable deduction. See *e.g. McGlotten* v. *Connally,* 338 F. Supp. 448, 456 (D.D.C. 1972), which declared unconstitutional tax advantages granted to a fraternal order which denied membership to non-white applicants. Chief Judge Bazelon, writing for a Three-Judge District Court, appropriately noted:

> "The rationale for allowing the deduction of charitable contributions has historically been that by doing so, the Government relieves itself of the burden of meeting public needs which in the absence of charitable activity would fall on the shoulders of the Government. 'The Government is compensated for its loss of revenue by its relief from financial burdens which would otherwise have to be met by appropriations from public funds.' H. Rep. No. 1860, 75th Cong. 3rd Sess. 19 (1938)."

Although the above discussion in *McGlotten* focused on § 170 deductions allowed donors, it can hardly be disputed that the granting of tax exempt status to charities, pursuant to § 501(c)(3), rests upon the same foundation.

In view of the foregoing the Court has no trouble in concluding that plaintiffs have adequately shown that, by reason of Revenue Ruling 69-545, they have suffered injury to an interest cognizable under and protected by the "charitable" provisions of the Internal Revenue Code. The second prong of the *SCRAP* test having thus been satisfied, standing is conferred upon plaintiffs to maintain this suit.

One further observation on the standing issue seems appropriate. As a general rule, Federal court inquiry into the propriety of tax policy stems from "refund" litigation instituted by disgruntled taxpayers. Standing in those cases presents no serious problem. However, in this situation it is quite obvious that since the contested Ruling in every respect establishes criteria quite favorable to persons whose tax status will be affected, its validity could not, in all probability, be tested in that normal course.

If the circumstances were reversed, i.e., were the most stringent provisions of Rev. Rul. 56-185 to overrule those of Rev. Rul. 69-545—taxpayers denied deductions, and hospitals refused tax exempt status, would be afforded the opportunity of challenging the Ruling upon which that tax liability had been predicated. Indeed, those litigants would be able to make the very sort of argument plaintiffs in this suit have presented, namely that the Ruling is contrary to statute and therefore without effect. The fact that the administration of Revenue Ruling 69-545 will not produce protesting taxpayers eager to challenge its

policy and application should not immunize the Ruling from such a testing where, as shown earlier, the Code policy it purports to serve has a fundamental purpose of aiding and benefiting the class of people to which plaintiffs belong.

The Court is not unmindful of and shares the government's concern for maintaining an efficient tax structure free from potential disruption from challenges by citizens for whom that policy has no actual tax consequence. However, the case *sub judice* presents somewhat of a unique situation in that the tax law in question also bears an identifiable relationship to citizens other than those whose tax returns are immediately affected.

It is also within the context that the Court, following the principles enunciated in *McGlotten* v. *Kennedy, supra* at 452–54, concludes that the "Federal taxes" exemption to the Declaratory Judgment Act, 28 U.S.C. § 2201 and the Tax Injunction Act, 26 U.S.C. § 7421(a) do not bar this suit.[15]

AUTHORITY TO PROMULGATE REVENUE RULING 69–545

As indicated at the outset, the defendants have maintained that the Commissioner's action is not subject to review by this Court, basing this central theme upon the "discretionary action" exception to the APA, 5 U.S.C. § 701(a)(2) which provides that:

> This chapter applies, according to the provisions thereof, except to the extent that . . .

[15] In McGlotten, the purposes of the above restrictions on litigation—the smooth and efficient assessment and collection of taxes—were held not to have been jeopardized by plaintiffs' challenge to the constitutionality of IRS policy. That reasoning is equally applicable in this suit.

(2) agency action is committed to the agency discretion by law.[16]

The Court, however, finds this provision to be inapplicable.

The Supreme Court has recently held this exception to be "* * * very narrow * * * applicable in those rare instances where 'statutes are drawn in such broad terms that in a given case there is no law to apply.' S. Rep. No. 752, 79th Cong., 1st Sess. 26 (1945)." *Citizens to Preserve Overton Park* v. *Volpe,* 401 U.S. 402, 410 (1971). To be sure, almost every administrative ruling, to some degree, flows from discretionary power vested in the executive branch. But the self-categorization of a decision as being "discretionary" does not of itself preclude court scrutiny under § 701(a)(2). The limited scope of that subsection is further evidence by § 706 of the APA, titled "Scope of Review," the terms of which empower a reviewing tribunal to vacate administrative determinations for "abuse of discretion." The obvious implication of that provision, as Professor Jaffe has observed, is that agency action is reviewable: " * * * *the presence of discretion should not bar a court from considering a claim of illegal or arbitrary use of discretion.*" L. Jaffe, Judicial Control of Administrative Action, 374–75 (1965) [Emphasis in original].

The *Overton Park* Court keyed the applicability of this exception to whether, under a particular set of circumstances, there is law to be applied by the administrator, *supra,* 401 U.S. 410, 413, and in this vein it is difficult to imagine that the deliberative process from which the policy embodied in Revenue Ruling 69–545

[16] Subsection (a)(1) makes exception from the general rule allowing for review where "statutes preclude judicial review." The government places no apparent reliance upon this provision.

emerged could be properly conducted without at least some consideration and application of the legal principles attendant to the "charitable" sections of Internal Revenue Code. Indeed, the government's insistence that the action was merely interpretative undercuts its position that the Ruling falls within the § 701 (a)(2) exception to review. To interpret is to explain, or to tell the meaning of—when action has the effect of changing or altering the terms of a statute the limits of "interpretation" have been over-stepped. Any discretion incorporated into the IRS's authority to promulgate rules and regulations is necessarily limited by the understanding that Congress, not the Treasury, is responsible for the formulation and institution of basic tax policy. It is true, as a matter of jurisprudence and efficient tax administration, that courts have regularly paid deference to the expertise attributed to the IRS in tax related matters and therefore judicial interference has been reluctantly employed. However, this exhibition of restraint is predicated upon the assumption that administrative rulings will do no more than effectuate, implement and clarify the provisions of the Code which have been Congressionally enacted:

> "The power of an administrative officer or board to administer a federal statute and to prescribe rules and regulations to that end is not the power to make law—for no such power can be delegated by Congress—but the power to adopt regulations to carry into effect the will of Congress as expressed by the statute. A regulation which does not do this, but operates to create a rule out of harmony with the statute is a mere nullity." *Manhattan General Equipment Co.* v. *Commissioner,* 297 U.S. 129, 134 (1936).

See also *Dixon* v. *United States,* 381 U.S. 68, 74–75 (1965) for a more recent application of this principle.

When this assumption is proven wrong, the courts must act to rectify any administrative determination which is not in accord with the Code. The Ruling is therefore reviewable.

Section 706 of the APA sets forth the standards for judicial inquiry, obligating ". . . the reviewing court to engage in a substantial inquiry,"[17] the initial step of which is to determine whether the administrator "acted within the scope of his authority." *Overton Park, supra* at 415, (citations omitted)

The Court turns for guidance to several recent Supreme Court rulings which, although not brought

[17] Section 706 provides:

"To the extent necessary to decision and when presented, the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of an agency action. The reviewing court shall—

"(1) compel agency action unlawfully withheld or unreasonably delayed; and

"(2) hold unlawful and set aside agency action, findings, and conclusions found to be—

"(A) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law;

"(B) contrary to constitutional right, power, privilege, or immunity;

"(C) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right;

"(D) without observance of procedure required by law;

"(E) unsupported by substantial evidence in a case subject to sections 556 and 557 of this title or otherwise reviewed on the record of an agency hearing provided by statute; or

"(F) unwarranted by the facts to the extent that the facts are subject to trial de novo by the reviewing court.

"In making the foregoing determinations, the court shall review the whole record or those parts of it cited by a party, and due account shall be taken of the rule of prejudicial error. Pub. L. 89-554, Sept. 6, 1966, 80 Stat. 393.

pursuant to the APA, are nonetheless instructive as to the contours of IRS authority.[18]

It is settled law that the positions adopted by the Treasury are presumptively valid and will not ordinarily be interfered with by the courts. *Bingler* v. *Johnson,* 394 U.S. 741, 750–51 (1969); *United States* v. *Correll,* 389 U.S. 299, 307 (1967).[19] That doctrine, however, is not automatically dispositive. As *United States* v. *Cartwright,* 411 U.S. 546, 550 (1973) admonished, it ". . . is to set the framework for judicial analysis; it does not displace it." The case of *Fribourg Nav. Co.* v. *Commissioner,* 383 U.S. 272 (1966) is particularly well suited to offer an analytical framework and will serve as a platform for this Court's examination.

At issue in *Fribourg* was the soundness of IRS policy, effectuated by a revenue ruling, concerning the sale of and deductions allowable for depreciable assets. An affected taxpayer litigated the issue to culmination with the Supreme Court declaring in his favor that the IRS position was contrary to the Code and therefore invalid. Although the actual holding is, of course, of no significance to the issues presented in this suit, the approach followed by the Supreme Court is. In reaching its determination, cognizance was taken and great weight was given to the fact that for many years the IRS had followed a fundamentally

[18] The cases generally followed the refund litigation route, which as earlier indicated, would not be available to these plaintiffs. See pages 11–12, *supra.*

[19] The Correll Court, in considering a challenge to a rule followed by the Commissioner of the Internal Revenue Service, held that: "The role of the judiciary in cases of this sort begins and ends with assuring that the Commissioner's regulations fall within his authority to implement the congressional mandate in some reasonable manner." 389 U.S. at 307.

different policy which had been solidified by court as well as congressional approval.

In *Cartwright, supra,* the Supreme Court adopted a similar line of reasoning when it invalidated a treasury regulation in which the criteria for determining the valuation of mutual fund holdings for federal estate tax purposes was established. After carefully noting that regulations are generally upheld, Mr. Justice White proceeded to hold that the regulation in question was an unrealistic and unreasonable interpretation of the Internal Revenue Code. Referring to the Investment Company Act of 1940, which regulates the mutual funds field, he concluded: "Congress surely could not have intended [the pertinent section of the Code] to be interpreted in such a manner." 411 U.S. at 577.[20]

The reasonableness of Revenue Ruling 69–545, and the policy announced therein, therefore hinges upon whether or not it is in accord with the terms of the Code. As is usually the case, there is no clear cut disparity between the administrative ruling and the statutory language, making it necessary for the Court to discern the intended meaning and proper interpretation of the pertinent provisions. Following *Fribourg,* the Court will focus upon and give careful consideration to the relevant judicial, legislative [21] and adminis-

[20] The Court adopted the position of a dissenting member of the Tax Court which had earlier dealt with the challenged Regulations:

"It does not follow that, because [the Commission] has a choice of alternatives, his choice should be sustained where the alternative chosen is unrealistic. In such a situation the regulations embodying that choice should be held to be unreasonable." 411 U.S. at 557, quoting from Estate of Wells v. Commissioner, 50 T.C. 871, 878 (1968).

[21] The significance of legislative intent is further conspicuously revealed in Bingler v. Johnson, *supra.* Although the Congressional history concerning the section of the Code there

trative history. This provides little, if any, support for the government's position.

The defendants do not dispute that Revenue Ruling 69–545 represented, as did the revenue ruling in *Fribourg,* a clear change of previously administered policy. And the Court does not mean to imply that the Commissioner should be so inflexible as to be required, under all circumstances, to rigidly adhere to past practices. However, he may not do so without sound basis and authority. As Justice White, in his *Fribourg* dissent, observed:

> "We have frequently in the past recognized the Commissioner's authority to re-evaluate a prior position upon the basis of greater experience and reflection and to adjust that position to the extent that he becomes convinced that an adjustment is necessary *to comport with congressional intent,* even when this results in a distinct reversal of a previous position * * *." 383 U.S. at 297 (citations omitted; emphasis added).

The government has attempted to justify the reversal of policy as to § 501(c)(3) with reference to Professor Scott's treatise on Trusts as well as the Restatement of Trusts, for which Scott is the Reporter. Rev. Ruling 69–545 itself includes such a reference.[22] Urging that modern day "community

involved (§ 117 exclusions from income of scholarships and fellowships) was by no means crystal clear, the Court nonetheless embarked upon an analysis of the relevant congressional history, determined what it considered to be the legislature's apparent reasoning and finally ruled that the contested Treasury Regulation comported with that meaning.

[22] "In the general law of charity, the promotion of health is considered to be a charitable purpose. Restatement (Second), Trust, Sec. 368 and Sec. 372; IV Scott on Trusts (3rd Ed. 1967), Sec. 368 and Sec. 372." Rev. Rul. 69–545.

benefit" concepts of charity, viewed in conjunction with the importance of promoting general health care, serve as a sufficient and rational basis for the IRS policy,[23] the Ruling is defended as a perfectly permissible interpretative determination. For judicial support reliance is placed upon *Green* v. *Connally*, 330 F. Supp. 1150 (D.D.C. 1971) where Circuit Judge Leventhal, emphasizing federal and public policy considerations, ruled that private educational institutions that followed racially discriminatory practices towards students were precluded from enjoying tax benefits under §§ 501(c)(3) and 170(a) to (c). The defendants take much comfort in the following passage:

> "But clearly, the term 'charitable' is used 'in its generally accepted legal sense,' . . . and not in a street or popular sense (such as, e.g., benevolence to the poor and suffering) . . . . Thus 'strong analogy' can be derived from the general common law of charitable trusts at least for close interpretative questions . . . ." 330 F.Supp. at 1157 (citations omitted).

The emphasis given by the IRS to Scott's principles of trust law, which the Court has no reason to doubt, was misplaced and provides, even when taken in conjunction with *Green*, an insufficient basis, in view of prior legislative and judicial history, to justify the basic shift in policy. The *Green* opinion, which of course followed the Ruling and therefore served, only

[23] Two aspects of the Ruling have been noted in this regard: 1. that emergency rooms must remain available to *all* patients and 2. that persons who are able to pay by means of third party reimbursement must receive general hospital treatment. These conditions, however, are of no consequence to the Court's finding that the Service erred in effectuating the substantial changes found in the Ruling.

as an after-the-fact basis, while perhaps pertinent for general definitional considerations, can hardly justify the Commissioner's attempt to reform the Code on an issue which had acquired a significant degree of meaning and rationale of its own. It is unnecessary to repeat in full this background but it is important to emphasize that the Ruling was promulgated simultaneously with a flourish of Congressional activity on the subject, allowing one to conclude that the Service would have naturally looked to Congress for insight. The House Report, which included the controversial change, was proposed on August 4, 1969; Senate rejection came in mid-November; and House adoption of the Senate revision followed shortly thereafter.

It is readily apparent that the Ruling was issued before any *final* Congressional determination had been rendered. Although at the time of promulgation the House had adopted a measure which was supportive of the Ruling, the required Senate approval had not been given. The Senate Finance Committee, which reported on its version, not only clearly stated that the matter would once again be reviewed in conjunction with Medicare and Medicaid legislation, it also gave some indication that the Committee members thought the Ruling to be in conflict with the Code:

> "The Committee deleted from the bill those provisions which would have conformed the Code to the result reached by the 1969 Ruling." S. Rep. No. 91-552, 91st Cong. 1st Sess. 61 (1969).

The IRS cannot satisfactorily demonstrate, by reason of this legislative activity, that it was supplied with a sufficiently convincing expression of Congressional intent as to warrant implementation of the sweeping policy change embodied in the Ruling.

The defendants claim, however, that Congress, being

fully aware of the Ruling and its consequence, granted implied approval by failing to affirmatively reject it. The Court finds this argument unpersuasive. The legislative record, even if viewed in the light most favorable to the government, reveals that the Congress, which was by no means silent on the issue, felt uncertainty and doubt as to the propriety of the Ruling. Nor has the Court been apprised of anything to indicate that the Senate was amenable to the House provisions which it deleted but felt that, in view of the Ruling, any further legislative action would be superfluous.

In short, any reading of the sequence of events to establish Congressional affirmation of the Ruling is less than persuasive and is an unacceptable basis for upholding its validity.

Accordingly, the Court finds that Revenue Ruling 69–545 was improperly promulgated and is without effect inasmuch as it allows private non-profit hospitals to qualify as charities under the Internal Revenue Code of 1954 without requiring the hospitals to offer special financial consideration to persons unable to pay.[24]

In view of the above holding the Court need not reach due process questions presented under the Fifth Amendment and the Administrative Procedure Act.

Counsel for plaintiffs shall present an appropriate order within 10 days.

BARRINGTON D. PARKER,
United States District Judge.

DECEMBER 20, 1973.

[24] The Court recognizes that Revenue Ruling 69–545 makes reference only to § 501(c)(3) and not to § 170. The Court has assumed, and the government has not argued to the contrary, that since the underlying policy considerations behind the "charitable" provisions of both sections are the same, conditions and requirements of § 501(c)(3) would apply equally to § 170.

United States District Court for the District of Columbia

Civil Action No. 1378–71

EASTERN KENTUCKY WELFARE RIGHTS ORGANIZATION, ET AL., PLAINTIFFS

v.

GEORGE P. SHULTZ, ET AL., DEFENDANTS

ORDER AND JUDGMENT

Plaintiffs and defendants have filed cross-motions for summary judgment concerning the legal obligations of defendants under the Internal Revenue Code with respect to the status, under sections 501(c)(3) and 170(a)–(c) of the Internal Revenue Code of 1954 (Title 26 U.S.C.), of nonprofit hospitals which refuse admission and services to persons unable to pay. Having had full opportunity to consider said motions, pleadings, affidavits, and memoranda, and after hearing argument, the Court for the reasons set forth in the Opinion filed on December 20, 1973, determines that there is no material issue of fact in dispute, and expressly directs the entry of a judgment in favor of plaintiffs as follows:

I. DECLARATORY RELIEF

Declared:

1. That the defendants acted outside their scope of authority under the Internal Revenue Code of 1954 (Code) by promulgating Revenue Ruling 69–545 inasmuch as that Ruling removed previously followed

requirements, found in Revenue Ruling 56–185, that private nonprofit hospitals seeking tax exempt status as charitable organizations under § 501(c)(3) of the Code must provide free or below cost treatment to individuals unable to pay for such services.

2. That Revenue Ruling 69–545, to the extent that it modifies Revenue Ruling 56–185 with regard to the requirements relating to the caring for patients without charge or at below cost rates, is void and without effect.

II. INJUNCTIVE RELIEF

Ordered, Adjudged and Decreed that defendants are hereby enjoined and restrained from:

1. Following the above voided policy contained in Revenue Ruling 69–545;

2. Granting tax exempt status under § 501(c)(3) of the Code and allowing deductions for contributions under § 170(a)–(c) of the Code to private nonprofit hospitals unless and until said hospitals:

a. Satisfy the requirements found in Revenue Ruling 56–185, in particular, that they: (1) be operated, to the extent of their financial ability, for those not able to pay for services and not exclusively for those who are able and expected to pay; (2) furnish the above "charitable" services on a reduced rate and below cost or no charge basis; (3) not refuse patients in need of hospital care who cannot pay.

b. Conspicuously post, in appropriate accessible public areas, notice, to be prepared by the defendants and subject to Court approval, which shall include:

(1) That the hospital has applied for or has been granted tax exempt status under § 501(c)(3) of the Code;

(2) An intelligible recitation of the previously mentioned provisions of Revenue Ruling 56–185.

The defendants shall take the necessary and immediate steps to implement this Order, including but not limited to revoking the voided portion of Revenue Ruling 69–545 and promulgating in its stead appropriate Rulings, and shall report their progress to the Court within 60 days of the entry of this Order, and at such further time as the Court deems necessary.

The Court will retain jurisdiction over this case during said implementation.

BARRINGTON D. PARKER,
United States District Judge.

JANUARY 28, 1974.

Copies to:

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John J. McCarthy, Esquire,
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Washington, D.C. 20530.

APPENDIX B

United States Court of Appeals for the District of Columbia Circuit

No. 74–1293

EASTERN KENTUCKY WELFARE RIGHTS ORGANIZATION, ET AL.

v.

WILLIAM E. SIMON, SECRETARY OF THE TREASURY, ET AL., APPELLANTS

Appeal From the United States District Court for the District of Columbia

(D.C. Civil No. 1378–71)

DECIDED OCTOBER 9, 1974

Wesley J. Filer, Attorney, Tax Division, Department of Justice, of the bar of the Supreme Court of Texas, *pro hac vice,* by special leave of court, with whom *Scott P. Crampton,* Assistant Attorney General, *Earl J. Silbert,* United States Attorney, and *Meyer Rothwacks* and *Leonard J. Henzke, Jr.,* Attorneys, Tax Division, Department of Justice, were on the brief, for appellants.

Marilyn G. Rose, with whom *Joseph Onek, Jeffrey B. Schwartz, Laurens H. Silver,* and *Anthony Z. Roisman* were on the brief, for appellees.

John A. Beck filed a brief on behalf of American Hospital Association as *amicus curiae* urging reversal.

Before WRIGHT and WILKEY, *Circuit Judges*, and JAMESON,* *Senior District Judge*.

Opinion for the court filed by *Senior District Judge* JAMESON.

Opinion concurring in part and dissenting in part filed by *Circuit Judge* WRIGHT.

JAMESON, *Senior District Judge:* Defendants-appellants, the Secretary of the Treasury and Commissioner of Internal Revenue, have appealed from an order granting summary judgment to plaintiffs-appellees and holding that "private nonprofit hospitals seeking tax exempt status as charitable organizations under § 501(c)(3) of the [Internal Revenue] Code must provide free or below cost treatment to individuals unable to pay for such services" and that a revenue ruling modifying this requirement is void.[1]

I. BACKGROUND

Sections 501(a) and (c)(3) of the Internal Revenue Code of 1954 (26 U.S.C. 501(a) and (c)(3) exempt from federal income tax: "(3) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for charitable . . . purposes, . . . no part of the net earnings of which inures to the benefit of any private shareholder or individual . . ." . Other related sections of the Code provide that contributions to such tax exempt charitable organizations are deductible for purposes of computing federal income tax (26 U.S.C. § 170) and estate and gift taxes (26 U.S.C. §§ 2055(a)(2), 2106 (a)(2)(A)(ii) and 2522(a)(2)).

*Of the United States District Court for the District of Montana, sitting by designation pursuant to 28 U.S.C. § 294(d) (1970).

[1] By order of this court, the American Hospital Association was granted leave to file briefs as *amicus curiae*.

Hospitals and other health organizations have never been expressly categorized as tax exempt organizations and have achieved that status only by qualifying as "charitable" organizations under the Code. Long established Internal Revenue Service (I.R.S.) policy held that hospitals qualified as charitable organizations under 501(c)(3) only if they provided free or below cost service to those unable to pay. This policy was articulated in Revenue Ruling 56–185, which held that a hospital could qualify for tax exempt status only if it was "operated to the extent of its financial ability for those not able to pay for the services rendered and not exclusively for those who are able and expected to pay".[2]

The I.R.S. modified this position in 1969 with the issuance of Revenue Ruling 69–545. The new ruling broadly defines "charitable" in terms of community benefit and holds that the promotion of health constitutes a "charitable purpose" in the "generally accepted legal sense of that term"[3] and within the meaning of § 501(c)(3) of the Code. According to the ruling,

> "The promotion of health . . . is one of the purposes in the general law of charity that is deemed beneficial to the community as a whole

[2] Other pertinent parts of Revenue Ruling 56–185 state: "It is normal for hospitals to charge those able to pay for services rendered in order to meet the operating expenses of the institution without denying medical care or treatment to others unable to pay. . . . It may furnish services at reduced rates which are below cost, and thereby render charity in that manner. . . . It must not, however, refuse to accept patients in need of hospital care who cannot pay for such services."

[3] As a basis for its conclusion that in the "general law of charity" the promotion of health is a charitable purpose, the I.R.S. relies on RESTATEMENT (SECOND) TRUSTS, sec. 368 and 372, and IV SCOTT ON TRUSTS (3rd ed. 1967) sec. 368 and 372.

> even though the class of beneficiaries eligible to receive a direct benefit from its activities does not include all members of the community, such as indigent members of the community . . .".

Based on this community benefit concept, a nonprofit hospital can qualify as a charitable organization under 501(a)(3) "By operating an emergency room open to all persons and by providing hospital care for all those persons in the community able to pay the cost thereof either directly or through third party reimbursement . . ." [e.g. private health insurance, Medicare, or Medicaid]. Thus, for a hospital to qualify as a tax exempt organization, the provision of free or below cost service to those unable to pay is no longer essential.[4]

Alleging harm from this new ruling, the plaintiffs-appellees, a group of health and welfare organizations and indigent persons, brought this action seeking to declare Revenue Ruling 69–545 invalid and to enjoin its implementation. They submitted affidavits recounting incidents in various parts of the country involving the denial of hospital services to indigents by institutions enjoying tax exempt status as "charitable" organizations.

Plaintiffs contended that (1) the Revenue Ruling constitutes an improper administrative alteration of the Internal Revenue Code in contradiction of long-standing Congressional tax policy and judicial interpretation; (2) the Ruling was not properly adopted due the I.R.S. failure to grant interested parties an opportunity to be heard, allegedly a violation of the Administrative Procedure Act and the Fifth Amend-

[4] Revenue Ruling 69–545 expressly states: "Revenue Ruling 56–185 is hereby modified to remove therefrom the requirements relating to caring for patients without charge or at rates below cost".

ment right of due process; and (3) the Ruling was an "abuse of discretion".

The defendants moved for dismissal of plaintiffs' complaint on the ground that the court lacked jurisdiction to entertain the action. The court denied this motion without opinion. Subsequently, upon the parties' cross motions for summary judgment, the court granted summary judgment in favor of the plaintiffs.

The court held:

(1) The plaintiffs have standing to maintain this action because they "have demonstrated sufficient injury flowing from the issuance of Revenue Ruling 69–545" and fall within the zone of interests protected by the Code.[5]

(2) The Federal tax exemption to the Declaratory Judgment Act, 28 U.S.C. § 2201, and the Tax Injunction Act, 26 U.S.C. § 7421(a), do not bar the suit.

(3) Judicial review of the Revenue Ruling is not precluded by the Administrative Procedure Act's provision in 5 U.S.C. § 701(a)(2) which forbids review of "agency action . . . committed to the agency discretion by law".

(4) The new Revenue Ruling does not comport with Congressional intent but rather is clearly contrary to the relevant judicial, legislative and administrative history on the matter. In light of this, the "community benefit" theory cannot "justify the basic shift in policy". The promulgation of the new ruling was therefore unauthorized.

[5] The district court, with respect to standing, noted that generally an action challenging a ruling of the Internal Revenue Service is in the nature of a refund action. The ruling challenged in this instance, however, is not one that will produce protesting taxpayers. The court concluded that this should not "immunize the Ruling" from judicial scrutiny, especially where, as here, the plaintiffs belong to a class of people whom the relevant sections of the Code purport to benefit.

CONTENTIONS ON APPEAL

Appellants level a dual attack against the judgment. First, they contend that the district court lacked jurisdiction in that the action is barred by (a) sovereign immunity, (b) the Anti-Injunction Act and the tax exemption to the Declaratory Judgment Act, and (c) the Administrative Procedure Act.[6] Second, appellants argue that Revenue Ruling 69–545 was authorized and does meet the charitable standard of § 501(c)(3) of the Code. In addition to opposing the contentions of appellants, appellees argue that the Revenue Ruling was not promulgated in accordance with the notice and hearing requirement of the Administrative Procedure Act and constitutes an abuse of discretion.

II. Jurisdiction

(a) *Sovereign Immunity*

The defense of sovereign immunity is jurisdictional. *See United States* v. *Sherwood*, 312 U.S. 584, 61 S.Ct. 767, 85 L.Ed. 1058 (1941). Generally, without specific authority, a court may not entertain an action against the sovereign. That doctrine, however, is not without its exceptions. The two primary exceptions were delineated in *Larson* v. *Domestic and Foreign Corp.*,

[6] The American Hospital Association in its *amicus* brief and appellants in note 46 of their brief contend also that appellees do not have standing because they have failed to demonstrate injury by an agency to an interest protected by the Code. This issue was discussed at length in the opinion of the district court. We agree with the court's conclusion that appellees made a sufficient showing of "injury in fact" to an interest "arguably within the zone of interests to be protected or regulated". *See, Sierra Club* v. *Morton*, 405 U.S. 727, 733, 92 S.Ct. 1361, 31 L.Ed.2d 636 (1972); *United States* v. *Students Challenging Regulatory Agency Procedures*, 412 U.S. 669, 93 S.Ct. 2405, 37 L.Ed.2d 254 (1973).

337 U.S. 682, 69 S.Ct. 1457, 93 L.Ed. 1628 (1949): sovereign immunity will not serve to bar jurisdiction when (1) the actions of a government official are beyond the scope of his authority or (2) "the statute or order conferring power upon the officer to take action in the sovereign's name is claimed to be unconstitutional". *Id.* at 689–690; *accord Dugan* v. *Rank*, 372 U.S. 609, 621–622, 83 S.Ct. 999, 10 L.Ed. 2d 15 (1963). Here plaintiffs alleged, and the district court found, that government officials had acted beyond their statutory power.

Appellants contend that (1) regardless of exceptions that may have been formulated in other judicial areas, sovereign immunity in matters of federal tax remains an absolute bar; (2) even if the *Larson* exceptions are viable in tax cases, the Commissioner was authorized by statute to interpret the term "charitable" as he did; and (3) mere error by the Commissioner in his interpretation of "charitable" would not negate the application of sovereign immunity, *Larson*, *supra* at 690.

Appellants rely on *Louisiana* v. *McAdoo*, 234 U.S. 627, 34 S.Ct. 938, 58 L.Ed. 1506 (1914) in support of their contention that the defense of sovereign immunity is absolute with respect to the area of federal taxes. *McAdoo* involved an action against the Secretary of the Treasury brought by the State of Louisiana as a sugar producer. Louisiana challenged the Secretary's determination of the tariff rates to be applied to sugar imported from Cuba. The Court held that the defense of sovereign immunity barred the action regardless of the fact that the State of Louisiana claimed that the action of the Secretary was not authorized by law.

McAdoo, however, must be viewed in its proper perspective. The Court decided that case in 1914. Since

then, significant changes have occurred in the area of standing, and exceptions to the doctrine of sovereign immunity have been judicially recognized. *Larson* and *Dugan, supra*. Moreover, with the advent of the Administrative Procedure Act in 1946, the continued viability of sovereign immunity with respect to administrative actions has been seriously questioned. *Scanwell Laboratories, Inc.* v. *Shaffer*, 424 F.2d 859, 873 (D.C. Cir. 1970).

The exceptions to the doctrine of sovereign immunity set forth in *Larson* have been applied in federal tax cases. In *McGlotten* v. *Connally*, 338 F.Supp. 448 (D. D.C. 1972), a nontaxpayer challenged the exempt status of a fraternal organization with racially discriminatory membership policies. The three-judge court rejected a sovereign immunity argument, holding that the "action falls readily within the two long-standing exceptions to that doctrine". *Id.* at 454, n. 27.[7] This court recognized the application of those exceptions in *Americans United* v. *Walters*, 477 F.2d 1169 (1973), reversed on other grounds *sub nom. Alexander* v. *Americans United*, —— U.S. ——, 94 S.Ct. 2053 (1974).[8]

The Government is correct in contending that "a claim of error" in the exercise of an officer's powers is not sufficient to invoke the scope of authority exce-

[7] The Government argues that *McGlotten* is either wrong or distinguishable in that it involved racial discrimination, a judicially sensitive issue. That the racial aspect was the controlling factor in the court's determination of *McGlotten* is not supported by the language of the decision.

[8] See also *Green* v. *Kennedy*, 309 F.Supp. 1127 (D. D.C. 1970), continued *sub nom. Green* v. *Connally*, 330 F.Supp. 1150 (D. D.C. 1971), *aff'd per curiam sub nom. Coit* v. *Green*, 404 U.S. 997, 92 S.Ct. 564, 30 L.Ed.2d 550 (1971); *Junior Chamber of Commerce of Rochester, Inc.* v. *The United States Jaycees*, 495 F.2d 883 (10 Cir. 1974).

tion to the sovereign immunity doctrine. *Larson, supra* at 690. Plaintiffs in this case, while not challenging the fact that the Secretary or Commissioner has the authority to prescribe rules and regulations for the administration of the revenue laws, nevertheless do challenge the authority of the Commissioner to interpret a revenue statute in a manner contrary to long-established Congressional policy. Thus, more than mere error on the part of the Commissioner is alleged. The court, therefore, has jurisdiction to determine whether or not the action of the Commissioner was authorized. The court has jurisdiction to determine its jurisdiction, *Land* v. *Dollar*, 330 U.S. 731, 739 (1947), even though such a determination requires a decision on the merits. *Larson, supra* at 690; *Bell* v. *Hood*, 327 U.S. 678, 682–683, 66 S. Ct. 773, 90 L. Ed. 939 (1946); *Junior Chamber of Commerce, supra*.

That sovereign immunity does not serve as a bar to the present action is further established by this court's position that the Administrative Procedure Act constitutes a waiver of sovereign immunity. Quoting from *Estrada* v. *Ahrens*, 296 F. 2d 690, 698 (5 Cir. 1961) this court in *Scanwell, supra* at 873 stated:

> "By providing judicial review in an action brought by 'any person adversely affected or aggrieved by any agency action' Congress permitted suits which under established tests would certainly be barred as suits against the government. . . . The Act thereby makes a clear waiver of sovereign immunity in actions to which it applies."

We conclude that the district court correctly held that the action was not barred by the doctrine of sovereign immunity.

(b) *Anti-Injunction and Declaratory Judgment Acts*

The Anti-Injunction Act (26 U.S.C. § 7421(a)) provides in relevant part: ". . . no suit for the purpose of

restraining the assessment or collection of any tax shall be maintained in any court by any person, whether or not such person is the person against whom such tax was assessed". In *Bob Jones University* v. *Simon*, —— U.S. ——, 94 S. Ct. 2038, 2046 (1974), the Court stated:

> "The Court has interpreted the principal purpose of this language to be the protection of the Government's need to assess and collect taxes as expeditiously as possible with a minimum of pre-enforcement judicial interference, 'and to require that the legal right to the disputed funds to be determined in suit for a refund.' *Enochs* v. *Williams Packing and Navigation Co.*, 370 U.S. 1, 7, 82 S. Ct. 1125, 1129, 8 L.Ed. 292 (1962)."

Here, the plaintiffs as nontaxpayers seek to have the I.R.S. enjoined from granting tax exempt status to hospitals which fail to provide free or reduced-charge services to indigents. The case of *McGlotten* v. *Connally*, *supra* is analogous. In *McGlotten* a black American brought a class action "to enjoin the Secretary of the Treasury from granting tax benefits to fraternal and nonprofit organizations which exclude non-whites from membership". *Id.* at 450. In rejecting the contention that the Anti-Injunction Act barred the suit, the court concluded that the action had "nothing to do with the assessment or collection of taxes. He [the plaintiff] does not contest the amount of his own tax, nor does he seek to limit the amount of tax revenue collectible by the United States. The preferred course of raising his objections in a suit for a refund is not available. In this situation we cannot read the statute to bar the present suit." *Id.* at 453–454.

The *McGlotten* rationale was followed by this court in *Americans United* v. *Walters*, 477 F. 2d 1169 (1973) in holding that a corporation in challenging the revocation of its tax exempt status was not attempting to restrain the assessment or collection of taxes. The Supreme Court, however, in *Alexander* v. *Americans United, Inc.*, — U.S. —, 94 S. Ct. 2053 (1974) reversed. The Court held that the purpose of the suit was to restrain the collection of taxes from contributors to the corporation. Accordingly, the Anti-Injunction Act applied and barred the action. The Court further stressed that an adequate legal remedy existed in the form of refund litigation.

Americans United, however, did not involve the factual situation presented in *McGlotten* and in this action. Here, as in *McGlotten*, rather than attempting to negate the levy of a tax, the plaintiffs are seeking to force the Government to impose a tax on contributions to certain hospitals. This, therefore, is not a case wherein the Government is faced with any threat to the actual assessment of collection of the taxes to which it deems itself entitled.

In addition, there is merit in the claim that there is no other adequate legal remedy.[9] Obviously neither the tax exempt charitable hospitals nor their contributors will institute refund litigation, as the contributions are tax free. It is apparent from a close analysis of the Anti-Injunction Act that it did not contemplate barring actions, such as this, where the litigation did not threaten to deny anticipated tax revenues to the Government.

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[9] In *Bob Jones*, *supra* at 2050, the Court stated: "This is not a case in which an aggrieved party has no access at all to judicial review. Were that true, our conclusion might well be different.

Appellants next contend that, even if the Anti-Injunction Act is held inapplicable, the tax exemption provision of the Declaratory Judgment Act (28 U.S.C. § 2261) bars the action. That provision authorizes federal courts to grant declaratory judgments "except with respect to Federal taxes". Appellants argue that the Declaratory Judgment Act is much broader in scope than the Anti-Injunction Act.

In *McGlotten*, *supra*, the court concluded that the Anti-Injunction Act and Declaratory Judgment Act are coterminous. This court in *Americans United*, *supra*, following the rationale of *McGlotten*, held that while the tax exemption provision of the Declaratory Judgment Act is literally broader than the Anti-Injunction Act provision, nevertheless the two are coterminous. The court reasoned that it would be paradoxical to authorize injunctive relief in some cases "while depriving courts the authority to declare the rights of the parties in connection with the injunctive relief". *Id.* at 1176.

Although the Supreme Court reversed *Americans United*, it did not deal with the issue of whether or not the Declaratory Judgment Act was broader than the Anti-Injunction Act.[10] A re-examination of the legislative history of the tax exemption provision leads this court to conclude, as it did in *Americans United*, that the Declaratory Judgment Act and the Anti-Injunction Act were intended to be coterminous.[11] Therefore, just as the Anti-Injunction Act does not bar this action, neither does the Declaratory Judgment Act.

[10] With respect to the question of whether the Declaratory Judgment Act is coterminous with the Anti-Injunction Act, the Court stated: "While we take no position on this issue, it is in any event clear that the federal tax exception to the Declaratory Judgment Act is at least as broad as the prohibition of the Anti-Injunction Act". 94 S.Ct. at 2057-2058, n. 10.

(c) *Administrative Procedure Act*

In contending that the Administrative Procedure Act precludes this action, appellants rely on 5 U.S.C. 701(a)(1), which indicates that administrative actions are not subject to review "to the extent that statutes preclude judicial review". With respect to this exception, the Supreme Court has held that access to judicial review will generally not be denied unless there is a showing by "clear and convincing evidence" of a contrary legislative intent. *Rusk* v. *Cort*, 369 U.S. 367, 379–380 (1962). Appellants argue that the Anti-Injunction Act, the tax exception to the Declaratory Judgment Act, and the doctrine of sovereign immunity, combined with specific procedures established

[11] When the Declaratory Judgment Act was passed in 1934, the Act did not contain the phrase "except with respect to Federal taxes", which now appears in § 2201. Some taxpayers used the Declaratory Judgment Act to do what they were prohibited from doing under the Anti-Injunction Act. *See, e.g. Penn* v. *Glenn*, 10 F.Supp. 483 (W.D. Ky. 1935), *app. dismissed per curiam*, 84 F. 2d 1001 (6 Cir. 1936), and *F. G. Vogt and Sons, Inc.* v. *Rothensies*, 11 F. Supp. 225 (E.D. Pa. 1935). Congress reacted to this by amending the Declaratory Judgment Act to include the tax exemption provision (Act of August 30, 1935, Ch. 829, § 405, 49 Stat. 1027). As noted by this court in *Americans United*, *supra* at 1176:

"The Senate Finance Committee, in reporting out the amended version, stated that the 'application of the Declaratory Judgments Act to taxes would constitute a radical departure from the long-continued policy of Congress [as represented today by § 7421(a)] with respect to the determination, assessment, and collection of Federal taxes.'"

With this legislative history it appears clear that Congress intended the Declaratory Judgment Act § 2201 to be coterminous with the Anti-Injunction Act.

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by Congress for review of tax matters, all indicate Congressional intent to "preclude judicial review".

We have concluded, however, that the Anti-Injunction Act, Declaratory Judgment Act and sovereign immunity do not bar this action. It is of course true, as appellants contend, that Congress has prescribed procedures for challenging administrative determinations of tax liability. Those procedures, however, are applicable only to cases involving the imposition of a tax, whereas here the challenge is made to a determination that certain hospitals are exempt from taxation as charitable organizations. We find no "clear and convincing evidence" that Congress intended to preclude judicial review in a case such as this.[12]

If anything, the pertinent Congressional enactments indicate a Congressional intent that the actions of the Internal Revenue Service be subject to judicial review.

[12] Appellants rely heavily on *National Railroad Passenger Corp. v. National Assn. of Railroad Passengers*, —— U.S. ——, 94 S. Ct. 690 (1974). That case involved the question of whether an organization representing railroad passengers could bring an action to enjoin the discontinuance of certain passenger trains operated by the National Railroad Passengers Corporation (Amtrak). The Court concluded that the private citizens had no right to bring the injunctive action. The case, however, is not in point. There is a significant difference between forcing the Government to incur deficits by requiring the continuance of train service and forcing the Government to tax contributions to certain hospitals. Furthermore, in *National Railroad* the legislative history of Amtrak Act indicated a Congressional intent to preclude private causes of action. *Id.* at 694. No such Congressional intent is to be found with respect to the Internal Revenue Code. Finally, Congress in the Amtrak Act expressly provided that the Attorney General should have the right to secure judicial review. Here no judicial review is possible except in an action by the plaintiffs.

The provision for review of the "assessment and collection" of taxes by the I.R.S. are the basis for many hundreds of taxpayer and I.R.S. suits every year. By means of refund and deficiency actions, the courts review the policies, practices, rulings, interpretations and actions of the Internal Revenue Service. Those cases cannot be commenced until after the assessment and collection of taxes. As noted *supra*, the rationale limiting suits to the post-collection period is not applicable in this case. To limit plaintiffs to a refund action under these facts is, as the district court concluded, equivalent to denying them judicial relief. That result is without foundation in the relevant law.

III. Validity of Revenue Ruling 69–545

In holding that "Revenue Ruling 69–545 was improperly promulgated and is without effect", the district court concluded that "based on relevant judicial, legislative, and administrative decisions" the new Ruling constituted an unauthorized reversal of a long-established policy of requiring exempt hospitals "to offer special financial consideration to persons unable to pay". The court recognized that "as a matter of jurisdiction and efficient tax administration . . . courts have regularly paid deference to the expertise attributed to the I.R.S. in tax related matters and therefore judicial interference has been reluctantly employed". The court continued: "However, this exhibition of restraint is predicated upon the assumption that administrative rulings will do no more than effectuate, implement and clarify the provisions of the Code which have been Congressionally enacted. . . . When this assumption is proven wrong, the courts must act to rectify any administrative determination which is not in accord with the Code."

We do not disagree with these principles of judicial interpretation of administrative rulings, but our own analysis of the judicial, legislative, and administrative decisions leads to a contrary result. We conclude that Revenue Ruling 69–545 is not inconsistent with 26 U.S.C. § 501(c)(3) and that the modification of the prior ruling was authorized.

The definition of the term "charitable" has never been static and has been broadened in recent years. Prior to 1959, Treasury Regulations generally defined charitable organizations as those operated for the relief of the poor.[13] In 1959, however, a comprehensive set of regulations interpreting § 501(c)(3) was issued.[14] These regulations adopted a broad concept of "charitable". The key provision, § 1.501(c)(3)–1(d)(2) reads:

> "(2) *Charitable defined.* The term 'charitable' is used in section 501(c)(3) in its generally accepted legal sense and is, therefore, not to be

[13] *See*, e.g. Treas. Reg. § 39.101(b)–1(b) (1939 Code) which stated:

"Corporations organized and operated exclusively for charitable purposes comprise, in general, organizations for the relief of the poor."

See also, I.T. 1800, II–2 Cum. Bull. 152 (1923), a ruling of the Commissioner of the I.R.S., which held that the term "charitable" in the predecessor of Section 501(c)(3) was used in its more restrictive sense of relief of the poor, rather than its broader legal sense in the law of charities.

[14] Revenue Ruling 56–185 was issued in 1956. Proposed regulations were also initially issued in 1956, repeating the restrictive view of charity contained in Ruling 56–185. (21 Fed. Reg. 460, 464 Jan. 21, 1956). These were withdrawn for more extensive study. The comprehensive set of regulations was proposed early in 1959 (24 Fed. Reg. 1421, 1423 Feb. 26, 1959) and, after public hearings, final regulations were issued, T.D. 6391, (24 Fed. Reg. 5217, 5219 June 26, 1959).

> construed as limited by the separate enumeration in section 501(c)(3) of other tax exempt purposes which may fall within the broad outlines of 'charity' as developed by judicial decisions. Such term includes: Relief of the poor and distressed or of the underprivileged; advancement of religion; advancement of education or science; erection or maintenance of public buildings, monuments, or works; lessening of the burdens of Government; and promotion of social welfare by organizations designed to accomplish any of the above purposes, or (i) to lessen neighborhood tensions; (ii) to eliminate prejudice and discrimination; (iii) to defend human rights secured by law; or (iv) to combat community deterioration and juvenile delinquency."

This Treasury Regulation was cited in *Green* v. *Connally, supra,* wherein the three-judge district court stated with respect to § 501(c)(3):

> "* * * clearly, the term 'charitable' is used 'in its generally accepted legal sense,' Treas. Reg. § 1.501(c)(3)–1(d)(2), and not in a street or popular sense (such as, e.g., *benevolence to the poor and suffering*). *See* H. Reiling, 'What is a Charitable Organization?' 44 A.B.A.J. 525, 527 (1958). Thus, 'strong analogy' can be derived from the general common law of charitable trusts, at least for close interpretative questions." 330 F. Supp. at 1157. (emphasis added).[15]

[15] The court said in part: "Changes in the courts' conceptions of what is charitable are wrought by changes in moral and ethical precepts generally held, or by changes in relative values assigned to different and sometimes competing and even conflicting interests of society." *Id.* at 1159.

In promulgating Revenue Ruling 69–545, the Commissioner did rely on an analogy to the law of charitable trusts. As indicated earlier, the Commissioner cited both the RESTATEMENT (SECOND) OF TRUSTS, sec. 368 and sec. 372,[16] and IV SCOTT ON TRUSTS (3rd ed. 1967) sec. 368 and sec. 372 [17] in holding that the promotion of health is a charitable purpose within the meaning of § 501(c)(3).

The term "charitable" is thus capable of a definition far broader than merely the relief of the poor. The law of charitable trusts supports the broader concept. The question involved here then is whether the term "charitable" as used in § 501(c)(3) may be broadly interpreted as was done in Revenue Ruling 69–545 or is to be restricted to its narrow sense of relief of the poor.

We cannot conclude, as did the district court, that Congress intended the latter construction. While it is true that in the past Congress and the federal courts have conditioned a hospital's charitable status on the level of free or below cost care that it provided for in-

[16] The RESTATEMENT (SECOND) OF TRUSTS sec. 368 (1959) states:

"Charitable purposes include: (a) the relief of poverty; (b) the advancement of education; (c) the advancement of religion; (d) *the promotion of health*; (e) governmental or municipal purposes; (f) other purposes the accomplishment of which is beneficial to the community." (emphasis added).

[17] SCOTT ON TRUSTS, 3rd. Ed. sec. 368 p. 2853 states "It is well settled that the promotion of health is a charitable purpose". Later in his treatise, Professor Scott observed that "a trust for the promotion of health, however, is nonetheless charitable although the benefits are not limited to the poor". Scott, *op. cit.* sec. 372, p. 2895.

digents,[18] there is no authority for the conclusion that the determination of "charitable" status was always to be so limited. Such an inflexible construction fails to recognize the changing economic, social and technological precepts and values of contemporary society.

In the field of health care, the changes have been dramatic. Hospitals in the early part of this nation's history were almshouses supported by philanthropy and serving almost exclusively the sick poor.[19] Today, hospitals are the primary community health facility for both rich and poor. Philanthropy accounts for only a minute percentage of the hospital's total operating costs.[20] Those costs have soared in recent years

[18] *Commissioner* v. *Battle Creek, Inc.*, 126 F.2d 405 (5 Cir. 1942); *Davis Hospital, Inc.*, 4 CCH Tax. Ct. Memo. 312 (1945); *Inter-City Hospital Association* v. *Squire*, 56 F. Supp. 472 (W.D. Wash. 1944); *Goldsby King Memorial*, 3 CCH Tax. Ct. Memo. 693 (1944); *Lorain Avenue Clinic*, 31 T.C. 141 (1958); *Robert C. Olney*, 17 CCH Tax Ct. Mem. 982 (1958); *Sonora Community Hospital*, 46 T.C. 519 (1966), *aff'd per curiam*, 397 F. 2d 814 (9 Cir. 1968).

[19] As noted by one commentator:

"General hospitals were established in the United States as early as the 18th century to serve the sick, poor and offer a roof and bed for the homeless or for those whose homes were inadequate. These institutions were primarily the last resort of the sick. Their standards of care did not approach those for the simplest custodial care today." John H. Hayes, ed., *Financing Hospital Care in the United States*, Vol. I, "Factors Affecting the Cost of Hospital Care" (1954), p. 9.

[20] Professor William Thomas speaking before a special Senate subcommittee in 1965 stated:

"The image of a voluntary institution as a charitable organization, financing its care of patients to a substantial degree through philanthropy * * * is largely anachronistic. Philanthropy, though increasing, has not been able to match the redoubled demands for health care." *Hearings on Conditions and Problems of the Nation's Nursing Homes*, Subcommittee on Long Term Care, Spec. Committee on Aging, U.S. Senate, 89th Cong., 1st Sess., Pt. 2 (Feb. 15, 1965), p. 559.

as constant modernization of equipment and facilities is necessitated by the advances in medical science and technology.[21]

The institution of Medicare and Medicaid in the last decade combined with the rapid growth of medical and hospital insurance has greatly reduced the number of poor people requiring free or below cost hospital services. Much of that decrease has been realized since the promulgation of Revenue Ruling 56–185. Moreover, increasingly counties and other political subdivisions are providing nonemergency hospitalization and medical care for those unable to pay.[22] Thus, it appears that the rationale upon which the limited definition of "charitable" was predicated has largely disappeared.[23] To continue to base the

[21] "Hospital expenses per patient day have increased over 700% since 1946, rising especially rapidly the last several years. * * * Among factors contributing to the rise in hospital expense are technological changes, increased demand, and rising costs of labor and supplies. * * * The public also demands more—a large number of more costly services—from the hospital now than it did two decades ago because of rising income, increasing insurance coverage, and changing demographic characteristics of the population." *Basic Facts on the Health Industry*, Committee on Ways and Means, 91st Cong., 1st Sess., June 28, 1971, p. 52.

[22] The Supreme Court, in holding unconstitutional a state statute requiring a year's residence in a county as a condition to an indigent receiving nonemergency hospitalization or medical care at the county's expense, referred to the "astronomical costs of hospitalization which bear so heavily on the resources of most Americans" and the fact that the "financial pressures under which private nonprofit hospitals operate have already led many of them to turn away patients who cannot pay or to severely limit the number of indigents they will admit". *Memorial Hospital* v. *Maricopa County*, 415 U.S. 250, 265 (1974).

[23] The state courts have recognized these changes in the health care field. As stated by the Supreme Court of Nebraska

"charitable" status of a hospital strictly on the relief it provides for the poor fails to account for these major changes in the area of health care.

In holding Revenue Ruling 69–545 void, the district court placed undue emphasis on the fact that Congress in 1969 failed to amend the Internal Revenue Code by including language which would have conformed the Code to the new ruling. The Senate Finance Committee in deleting a House provision which would have allowed exempt status to institutions "organized and operated exclusively for the providing of hospital care" stated:

> "The committee deleted from the bill those provisions which would have conformed the code to the result reached by the 1969 ruling. The committee decided to reexamine this matter in connection with pending legislation on Medicare and Medicaid." [24]

in *Evangelical Lutheran Good Samaritan Society* v. *County of Gage*, 181 Neb. 831, 151 N.W.2d 446, 449 (1967):

"Formerly all institutions furnishing services of this nature, including hospitals and nursing homes, were providing care for many patients without compensation and extended charity in the sense of alms-giving or free services to the poor. With the advent of present day social security and welfare programs, this type of charity is not often found because assistance is available to the poor under these programs. Yet, * * * the courts have defined 'charity' to be something more than mere alms-giving or the relief of poverty and distress, and have given it a significance broad enough to include practical enterprises for the good of humanity operated at a moderate cost to those who receive the benefits."

[24] Actually the provision of the House bill which was deleted provided a broader exemption than Revenue Ruling 69–545. It would have afforded exempt status to all nonprofit hospitals. Ruling 69–545 requires the operation of an emergency room open to all regardless of ability to pay as well as acceptance of Medicare and Medicaid patients and patients whose hospital costs will be paid by third parties.

This action or inaction by Congress cannot be interpreted as disapproving the new ruling. Congress could have rejected the ruling had it determined that it was not in conformity with the Code. Instead, it committed the matter for further study in the light of Medicare and Medicaid. No further action has been taken by Congress since the ruling became effective in 1969.

It is important to note also that Revenue Ruling 69–545 rather than overruling Revenue Ruling 56–185 simply provides an alternative method whereby a nonprofit hospital can qualify as a tax exempt charitable organization. That method entails the operation of an emergency room open to all regardless of their ability to pay and providing hospital services to those able to pay the cost either directly or through third party reimbursement. Thus, to qualify as a tax exempt charitable organization, a hospital must still provide services to indigents.

The required provision of emergency room services is of great import to the indigent. Emergency room service is often the only means of access that the poor have to medical care.[25] Furthermore, the fact that hospitals seeking to qualify as charities pursuant to Revenue Ruling 69–545 must accept Medicare and

[25] "Finding a physician and getting health care is particularly difficult for families who change communities. A significant portion of these are poor. When health needs become critical, families that do not have adequate financial resources may find the emergency rooms and outpatient clinics of general hospitals the only available resource. These families, along with poor families, who often have no other alternative, have contributed to the 150 million emergency room and outpatient visits in 1967, an increase of 250% during the past two decades." *National Advisory Commission on Health Facilities: A Report of the President* (1969), p. 20.

Medicaid patients is also significant. A large percentage of the indigent populace of the nation is now covered by either Medicare or Medicaid. In the final analysis, Revenue Ruling 69–545 may be of greater benefit to the poor than its predecessor Ruling 56–185.[26] Certainly Ruling 69–545 is more in conformity with the concept of "charitable" as defined in the Treasury Regulation adopted, after extensive study, in 1959 and interpreting § 501(c)(3).

In summary, we conclude that Revenue Ruling 69–545 is founded on a permissible definition of the term "charitable" and is not contrary to any express Congressional intent.

IV. Notice and Hearing Requirements of APA; Abuse and Discretion

Appellees contend that, if this court should find that the Commissioner was authorized to promulgate Revenue Ruling 69–545, the district court must nevertheless be sustained because appellants had the legal obligation under 5 U.S.C. § 553 to afford appellees an

[26] Moreover, Revenue Ruling 69–545 sets forth a more definite and specific standard. Under Revenue Ruling 56–185 hospitals were required to provide free care only to the extent of their financial ability. Hospitals operating at a deficit would have no obligation under Ruling 56–185. In addition the Ruling qualified the "financial ability" standard by providing:

"The fact that its charity record is relatively low is not conclusive that a hospital is not operated for charitable purposes to the full extent of its financial ability . . . . It may also set aside earnings which it uses for improvements and additions to hospital facilities. . . . A nominal charity record for a given period of time, in the absence of charitable demands of the community, will not affect its right to continued exemption."

opportunity to be heard.[27] They argue that Revenue Ruling 69–545 is a substantive rule as opposed to an interpretative ruling and therefore § 553 of the APA is applicable.

Section 553 of the Administrative Procedure Act expressly excepts interpretative rules from the notice and hearing requirements of the Act. This court distinguished interpretative and substantive rules in *Gibson Wine Co.* v. *Snyder*, 194 F.2d 329 (1952):

> "Generally speaking, it seems to be established that 'regulations', 'substantive rules' or 'legislative rules' are those which create law, usually implementary to an existing law; whereas interpretative rules are statements as to what the administrative officer thinks the statute or regulation means. . . . 'A substantive rule is one which . . . is intended to implement the statutory structure or the statutory powers of any agency. An interpretative rule is one which does not have the full force and effect of a substantive rule but which is in the form of an explanation of particular terms in an Act. If you had an expression in a statute such as 'Interurban Railway,' the query might come up as to what is an 'interurban railway'. A particular agency may adopt a rule defining an interurban railway. That, in a sense, may be called an interpretative rule.'" *Id.* at 331–332.[28]

Here the Commissioner interpreted the meaning of the term "charitable" in § 501(c)(3). The fact that the

[27] Having determined that the Revenue Ruling conflicted with Congressional intent, the district court did not reach appellees' contentions that the Ruling was promulgated without proper notice and hearing and constituted an abuse of discretion.

[28] *Accord, United States* v. *353 Cases, etc.*, 247 F. 2d 473, 480 (8 Cir. 1957).

term had been interpreted by the Commissioner differently in an earlier revenue ruling is not controlling. In the meantime Treasury Regulations containing a broader concept of "charitable" had been adopted in 1959, after notice and public hearings. In our opinion Internal Revenue 69–545 conforms to the definition of "charitable" set forth in these Regulations. Furthermore, appellants concede that Revenue Ruling 69–545 has no independent binding effect and that the courts are not bound by it unless they choose to accept it as a proper interpretation of the meaning of the word "charitable" as used in § 501(c)(3).[29] We conclude that Revenue Ruling 69–545 is an interpretative ruling and is not subject to the requirements of § 553 of the APA.[30]

Appellees finally contend that the promulgation of Revenue Ruling 69–545 constituted an abuse of discretion and should be set aside pursuant to U.S.C. 706 (2)(A).[31] Appellees argue that the Internal Revenue Service acted without considering all of the relevant factors. Their primary attack is again levelled at an alleged failure of the I.R.S. to consider the needs of the poor.

[29] *See, American President Lines, Ltd.* v. *Federal Maritime Commission*, 316 F. 2d 419, 421–422 and n. 5 (D.C. Cir. 1963).

[30] Appellees lay great stress on the facts that (1) Revenue Ruling 69–545 has a substantial impact on the availability of hospital services for the poor; (2) the I.R.S. is not an expert in health care delivery problems and thus needs to be educated; and (3) the Ruling constitutes a reversal of longstanding I.R.S. policy. While these factors have been considered by the courts with respect to whether notice and hearing are required by the APA, they are not determinative here where a ruling is clearly interpretative in nature and has no legally binding effect.

[31] 5 U.S.C. § 706(2)(A) authorizes courts to set aside agency actions found to be "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law".

We cannot agree. On its face, Revenue Ruling 69–545 indicates that the interests of the poor were considered. Emergency room treatment for all and acceptance of third-party reimbursement of hospital expenses were specifically established as conditions for tax exempt status under the Ruling. As indicated previously, both of those requirements substantially benefit the poor. Furthermore, the I.R.S. had before it a treasury regulation, 1.501(*c*)(3)–1(d)(2) *supra,* which expressly provided a broad definition of the term "charitable". In light of these factors and the changed health care situation in the country as a result of Medicare, Medicaid and other government programs, of which the I.R.S. was cognizant, the promulgation of Revenue Ruling 69–545 cannot be held to constitute an "abuse of discretion".

Reversed.

WRIGHT, *Circuit Judge, concurring in part and dissenting in part*: I concur in Part II of the court's opinion affirming the District Court on the jurisdictional issues raised on this appeal. On the merits I would also affirm the District Court for the reasons stated in its opinion holding Revenue Ruling 69–545 invalid. *See Eastern Kentucky Welfare Rights Organization* v. *Shultz,* D. D.C., 370 F. Supp. 325 (1973).

Assuming the defendants had the legal right to eliminate the requirement that nonprofit hospitals serve indigents in order to be eligible for "charitable" tax status under the Code, I would still find Revenue Ruling 69–545 invalid because it was issued without compliance with the informal rule-making procedures required by Section 553 of the Administrative Procedure Act, 5 U.S.C. § 553 (1970). Revenue Ruling 69–545 replaced Revenue Ruling 56–185 which provided that a hospital could qualify for tax exempt status

only if it was "operated to the extent of its financial ability for those not able to pay for the services rendered and not exclusively for those who are able and expected to pay." Revenue Ruling 69–545 provided "Revenue Ruling 56–185 is hereby modified to remove therefrom the requirements relating to caring for patients without charge or at rates below cost." Thus Revenue Ruling 69–545 worked a substantial change in the availability of hospital services for the poor. Yet, admittedly, neither the poor nor anyone else was given notice of the proposed change or allowed to comment on it.

The Internal Revenue Service is not expert in health care delivery needs and, consequently, was unable to draw on any expertise of its own in determining to free "charitable" hospitals from their obligations under existing IRS rulings to serve the poor. Comment from disciplines more directly related to health care and poverty could doubtless have assisted the IRS in deciding whether to relax the obligations of these hospitals to the poor. In proceeding without complying with the requirements of the Administrative Procedure Act, the IRS denied itself access to education which would have allowed it to make a more informed judgment. "Section 553 was enacted to give the public an opportunity to participate in the rule-making process. It also enables the agency promulgating the rule to educate itself before establishing rules and procedures which have a substantial impact on those regulated." *Texaco, Inc.* v. *FPC,* 3 Cir., 412 F.2d 740, 743 (1969).

570-027—75——5

APPENDIX C

United States Court of Appeals
for the District of Columbia Circuit

September Term, 1974—Civil Action 1378–71

No. 74–1293

EASTERN KENTUCKY WELFARE RIGHTS ORGANIZATION, ET–AL.

v.

WILLIAM E. SIMON, SECRETARY OF THE TREASURY, ET AL., APPELLANTS

Appeal from the United States District Court for the District of Columbia.

Before WRIGHT and WILKEY, Circuit Judges and JAMESON,* Senior District Judge for the District of Montana

JUDGMENT

This cause came on to be heard on the record on appeal from the United States District Court for the District of Columbia, and was argued by counsel.

On consideration thereof It is ordered and adjudged by this Court that the judgment of the District Court appealed from in this cause is hereby

*Sitting by designation pursuant to 28 U.S.C. § 294(d) (1970).

reversed, in accordance with the opinion of this Court filed herein this date.

Per Curiam

For the Court:

HUGH E. KLINE, *Clerk*.

Date: October 9, 1974.

Opinion for the Court filed by Senior District Judge Jameson.

Opinion concurring in part and dissenting in part filed by Circuit Judge Wright.

APPENDIX D

[NOTICE.—This opinion is subject to formal revision before publication in the Federal Reporter or U.S. App. D.C. Reports. Users are requested to notify the Clerk of any formal errors in order that corrections may be made before the bound volumes go to press.]

United States Court of Appeals for the District of Columbia Circuit

No. 74–1293

EASTERN KENTUCKY WELFARE RIGHTS ORGANIZATION, ET AL.

v.

WILLIAM E. SIMON, SECRETARY OF TREASURY, ET AL., APPELLANTS

Before BAZELON, *Chief Judge;* WRIGHT, MCGOWAN, TAMM, LEVENTHAL, ROBINSON, MACKINNON, ROBB AND WILKEY, *Circuit Judges.*

Filed December 6, 1974

ORDER

Appellees' suggestion that the matter be considered *en banc* having been circulated to the full court, and there not being a majority of the judges in regular active service in favor of having this case reheard *en banc,* it is

ORDERED by the court *en banc* that appellees' aforesaid suggestion is denied.

Per Curiam

Statement of BAZELON, *Chief Judge,* with whom Circuit Judges WRIGHT and ROBINSON concur, as to why he voted to grant rehearing *en banc.*

Statement of WRIGHT, *Circuit Judge,* with whom Chief Judge BAZELON and Circuit Judge ROBINSON concur, as to why he voted to grant rehearing *en banc.*

Statement of BAZELON, *Chief Judge,* as to why he voted to grant rehearing *en banc:*

I concur in Judge Wright's dissent and statement as to why he voted to grant rehearing *en banc* on the issue of compliance with the rulemaking procedures of the Administrative Procedure Act, 5 U.S.C. § 553 (1970). I add only this further thought. The panel opinion concedes, as it must, that rulemaking procedures are required if Rev. Rul. 69–545 has an "independent binding effect." If the Rev. Rul. were no more than "an opinion of the legal staff" of the Treasury,[1] I might agree with the majority that courts "are not bound by [the Revenue Ruling] unless they choose to accept it" and that, therefore, the Rev. Rul. has no independent binding effect. But in light of the traditional deference to Internal Revenue Service regula-

[1] American President Lines, Ltd. v. Federal Maritime Comm'n, 316 F. 2d 419, 422 (D.C. Cir. 1963). *See* Hou Ching Chow v. Attorney-General, 362 F. Supp. 1288, 1292 (D.D.C. 1973); Continental Oil Co. v. Burns, 317 F. Supp. 194 (D. Del. 1970). *Cf.* Pacific Gas & Elec. Co. v. FPC, Nos. 73–1358, –1485 (D.C. Cir. June 26, 1974) at 8–9 n.14, 10–13 (slip opinion); Lewis-Mota v. Secretary of Labor, 469 F. 2d 478 (2d Cir. 1972); California Citizens Band Ass'n v. United States, 375 F. 2d 43 (9th Cir.), *cert. denied,* 389 U.S. 844 (1967). There is nothing in Gibson Wine Co. v. Snyder, 194 F. 2d 329 (D.C. Cir. 1952), which is inconsistent with these cases. There is, I think no one would doubt, a very substantial difference between regulations defining a type of grape and regulations interpreting such legislative phrases as "the public interest" or "tax avoidance purpose."

tions in the interpretation of the more general sections of the Internal Revenue Code of 1954,[2] I think it a truly heroic assumption that courts will not be bound by the Ruling "unless they choose to accept it."

Indeed, this tradition of deference informs the panel majority's own approach to the legality of Rev. Rul. 69–545. The majority does not review the issue *de novo* but instead concludes that the Ruling "is founded on a *permissible* definition of the term 'charitable' and is not contrary to any *express* Congressional intent."[3] If the majority were to review the issue *de novo,* it would, I take it, certainly want more information than is contained in the record before us here. And it is for expressly that reason, as Judge Wright so persuasively argues, that rulemaking hearings are required.[4] So the majority tells the plaintiffs that it will not be bound by the Internal Revenue Service interpretation of the term "charitable" and then turns right around and upholds the Service interpretation as a permissible exercise of discretion on the basis of factual assumptions which are not supported by a record and which plaintiffs have not had an opportunity to rebut. I will not concur in such reasoning.

[2] *See* United States v. Cartwright, 411 U.S. 546, 550 (1973); Bingler v. Johnson, 394 U.S. 741, 749–51 (1969); Comm'r v. South Texas Lumber Co., 333 U.S. 496, 501 (1948); Comm'r v. O. Liquidating Co., 292 F. 2d 225, 231 (3d Cir.), *cert. denied,* 368 U.S. 898 (1961); Kern v. Granquist, 291 F. 2d 29, 32 (9th Cir. 1961). *Compare* Kurzner v. United States, 413 F. 2d 97, 112 (5th Cir. 1969) *with* O'Neill v. United States, 410 F. 2d 888 (6th Cir. 1969).

[3] Slip op. at 23 (emphasis added).

[4] *See also* NLRB v. Wyman-Gordon Co., 394 U.S. 759, 775–80 (1969) (Douglas, J. dissenting).

Statement of *Circuit Judge* WRIGHT as to Why He Voted to Grant Rehearing *En Banc:*

Revenue Ruling 69–545, which the panel majority upholds, replaced Revenue Ruling 56–185 which provided that a hospital could qualify for tax exempt status only if it was "operated to the extent of its financial ability for those not able to pay for the services rendered and not exclusively for those who are able and expected to pay." Revenue Ruling 69–545 provides: "Revenue Ruling 56–185 is hereby modified to remove therefrom the requirements relating to caring for patients without charge or at rates below cost." Thus Revenue Ruling 69–545 worked a substantial change in the availability of hospital services for the poor. Yet, admittedly, neither the poor nor anyone else was given notice of the proposed change or allowed to comment on it.

On the basis of assumed social, economic, and technological changes in the need of the poor for free medical care, the panel majority approves Revenue Ruling 69–545. The record in this case does not reflect what the needs of the poor for free medical care really are because the Internal Revenue Service did not comply with the rule-making procedures required by Section 553 of the Administrative Procedure Act, 5 U.S.C. § 553 (1970). Thus millions of poor people are effectively denied medical care without the procedural protections provided by law. If these procedural protections had been provided, doubtless it would have been disclosed that millions of Americans are indeed to poor to pay for hospital services and have no means of obtaining those services except as charity patients at our nonprofit hospitals. With this fact established as a matter of record, I confidently believe that Revenue Ruling 69–545 would never have been promulgated in the first place.

I would affirm the District Court in this case for the reasons stated in its opinion holding Revenue Ruling 69–545 invalid (*see Eastern Kentucky Welfare Rights Organization* v. *Shultz,* D. D.C., 370 F. Supp. 325 (1973)). I would also hold Revenue Ruling 69–545 invalid because it was issued without compliance with the rule-making procedures required by Section 553 of the Administrative Procedure Act, 5 U.S.C. § 553, as indicated in my dissent to the panel opinion.

United States Court of Appeals for the District of Columbia Circuit

No. 74-1293

September Term, 1974—Civil Action 1378-71

EASTERN KENTUCKY WELFARE RIGHTS ORGANIZATION, ET AL.

v.

WILLIAM E. SIMON, SECRETARY OF THE TREASURY, ET AL., APPELLANTS

Before WRIGHT and WILKEY, *Circuit Judges;* JAMESON,* U.S. Senior District Judge for the District of Montana

ORDER

On consideration of appellees' petition for rehearing, it is

ORDERED by the Court that appellees' aforesaid petition is denied.

For the Court:

HUGH E. KLINE, *Clerk.*

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*Sitting by designation pursuant to Title 28 U.S. Code Section 294(d).

Circuit Judge Wright would grant rehearing for the reasons set forth in his statement as to why he voted to grant rehearing, *en banc.*

APPENDIX E

Internal Revenue Code of 1954 (26 U.S.C.):

SEC. 170. CHARITABLE, ETC, CONTRIBUTIONS AND GIFTS.

* * * * *

(c) [as amended by Sec. 201(a), Tax Reform Act of 1969, P.L. 91-172, 83 Stat. 487, 553] *Charitable Contribution Defined.*—For purposes of this section, the term "charitable contribution" means a contribution or gift to or for the use of—

* * * * *

(2) A corporation, trust, or community chest, fund, or foundation—

(A) created or organized in the United States or in any possession thereof, or under the law of the United States, any State, the District of Columbia, or any possession of the United States;

(B) organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes or for the prevention of cruelty to children or animals;

(C) no part of the net earnings of which inures to the benefit of any private shareholder or individual; and

(D) no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

A contribution or gift by a corporation to a trust, chest, fund, or foundation shall be deductible by reason of this paragraph only if

it is to be used within the United States or any of its possessions exclusively for purposes specified in subparagraph (B).

* * * * *

SEC. 501. EXEMPTION FROM TAX ON CORPORATIONS, CERTAIN TRUSTS, ETC.

* * * * *

(c) *List of Exempt Organizations.*—The following organizations are referred to in subsection (a):

* * * * *

(3) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

* * * * *

SEC. 7421. PROHIBITION OF SUITS TO RESTRAIN ASSESSMENT OR COLLECTION.

(a) [as amended by Sec. 110(e), Federal Tax Lien Act of 1966, P.L. 89-719, 80 Stat. 1125, 1144] *Tax.*—Except as provided in sections 6212 (a) and (c), 6213(a), and 7426 (a) and (b)(1), no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court by any person, whether or not such person is the person against whom such tax was assessed.

* * * * *

28 U.S.C.:

§ 2201. *Creation of remedy.*

In a case of actual controversy within its jurisdiction, except with respect to Federal taxes, any court of the United States, upon the filing of an appropriate pleading, may declare the rights and other legal relations of any interested party seeking such declaration, whether or not further relief is or could be sought. Any such declaration shall have the force and effect of a final judgment or decree and shall be reviewable as such.

§ 2202. *Further relief.*

Further necessary or proper relief based on a declaratory judgment or decree may be granted, after reasonable notice and hearing, against any adverse party whose rights have been determined by such judgment.

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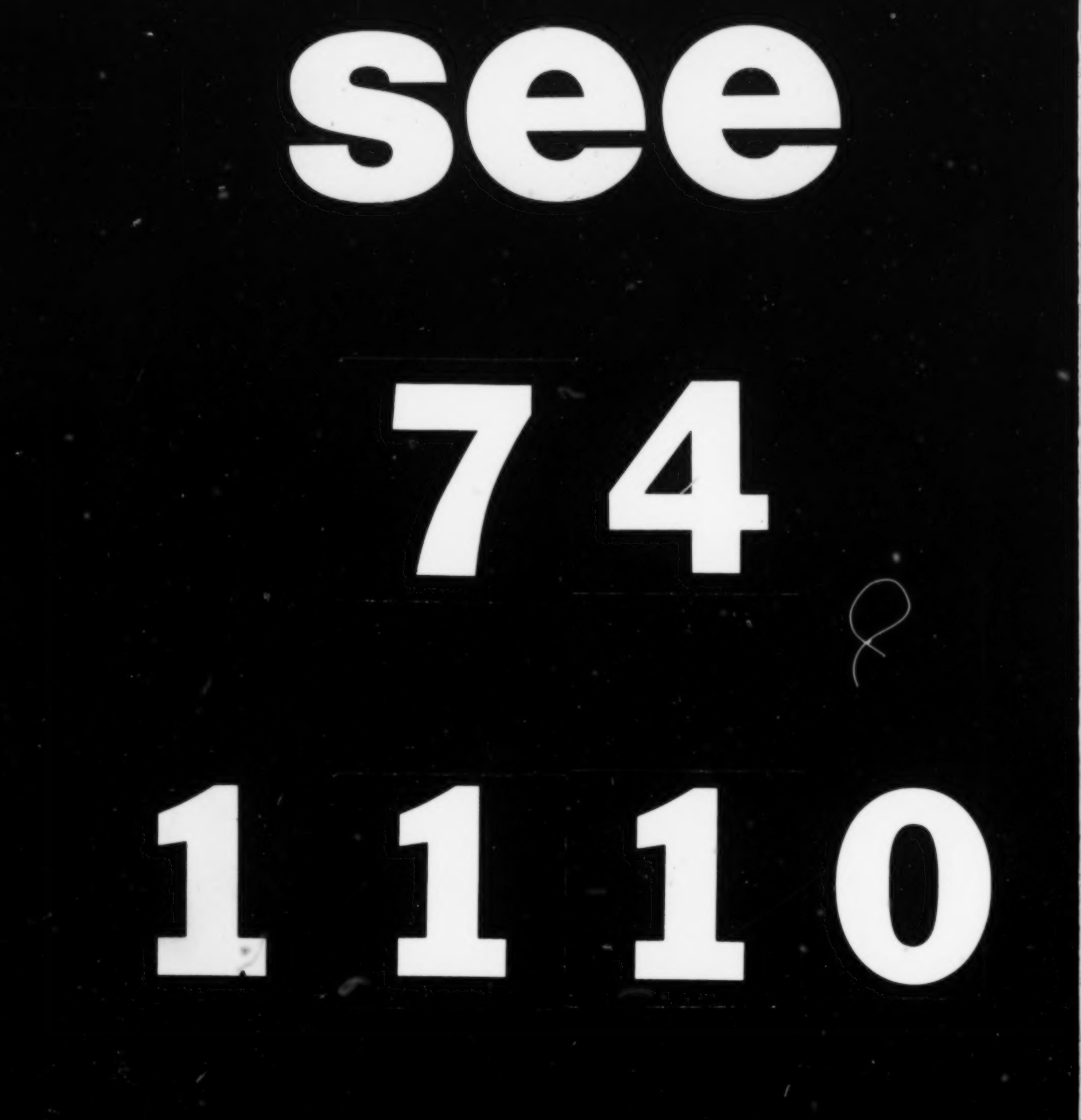
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